Economic Impact Analysis: A Case Study

Local Merchants vs. Chain Retailers

COMPLETE REPORT

Prepared for

liveablecity

&

A.I.B.A. Austin Independent Business Alliance — Supporting Locally-Owned Business

by

Civic Economics

Creativity · Opportunity · Prosperity

December 2002

INTRODUCTION

Civic Economics is pleased to present Liveable City with this Economic Impact Analysis assessing the economic impact of local merchants relative to a chain merchant carrying comparable lines of goods. Sixth and Lamar, specifically BookPeople, Waterloo Records, and Borders Books & Music, provide a case study.

The National Context

American communities from coast to coast have wrestled with the implications of national chain retail. In many small communities, the issue comes to a head with the imminent arrival of a large discount store, and manifests itself in an anti-Wal-Mart campaign. In others, the desperate quest for sales tax revenues places public officials squarely on the side of national merchants. Few would argue that chain stores have no place in a large community such as Austin. In many cases these stores expand consumer choice and offer good consumer value.

Despite national interest, however, CivEc has identified a near absence of objective, fact-based analysis of the phenomenon. Proponents and opponents alike present broad arguments based on emotional or philosophical pleas, for “mom and pop” shops and local character on one side and for free markets and consumer choice on the other. This report is designed to enhance the discussion by providing a credible and quantifiable analysis.

The Local Context

The area of Sixth Street and Lamar Boulevard in central Austin provides an outstanding opportunity to study the dynamics of retail competition. The following analyses are put forth as a case study of the interaction among co-locating chain and local merchants in similar lines of goods.

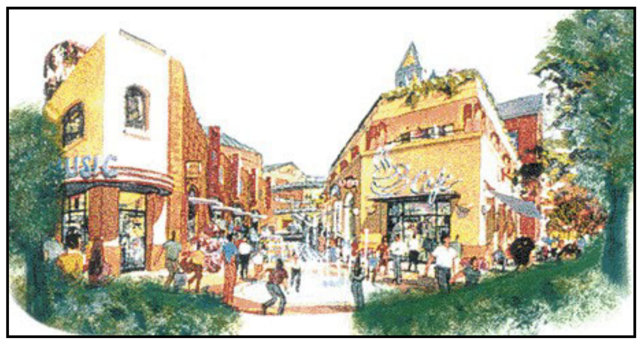
There can be no doubt that development of the properties in question is in the public interest. The corner of Sixth and Lamar is destined to become a retail, residential, and office hub for the region. Austin policymakers have wisely promoted this outcome. However, few seriously contend that the composition of this development is unimportant. Austin’s smart growth, great streets, and downtown development policies are carefully crafted to promote the health of the city by providing developers with incentives for preferred behaviors.

This analysis demonstrates a clear failure of public policy to steer desirable development at the site in question. As presently configured, new development at the corner will yield a net loss to the local economy. Moreover, previous decisions have placed the city in the position of subsidizing such an outcome.

Schlosser Development Corp. presently controls the two blocks between Fifth and Sixth to the east of Lamar as well as the previously developed block to the south, containing Office Max, Starbucks, and an AT&T Phone Store. Should the development proceed as presently structured, Schlosser will additionally take on leasing responsibilities at the present Whole Foods and BookPeople complex.

Under the present proposal, the offices and flagship store of Whole Foods Market will occupy the prime block of the Schlosser site. Whole Foods is a genuine Austin success story, growing in 20 years from a single Lamar store to a national chain with 137 outlets and growing. Whole Foods became a publicly traded company in 1992 (Nasdaq: WFM). Much of the company's expansion has come through acquisition of 12 local chains around the nation.

Schlosser proposes to anchor the eastern block with a Borders Books & Music store. Borders, like Whole Foods, is a hometown success story in a college town. From the first store in Ann Arbor, Borders has grown into the second largest national retailer of books and music. After a brief stint as a subsidiary of K-Mart, Borders was spun out in 1997 and now trades as BGI, the holding company for Borders and Waldenbooks.



As originally presented to the City, the Schlosser development on the site was to be an "urban village," albeit one with a Target store for an anchor. This proposal (at left), featuring the design work of internationally recognized Jerde Partnership, was approved for substantial public incentives. Unfortunately, after clearing and grading the site and closing a public street, the project was postponed due to financing difficulties. The project was resurrected in the summer of 2002 in the present configuration.

According to published sources, the combined Schlosser properties have been granted incentives with a total value of over $2.1 Million. These include fee waivers, water and wastewater infrastructure reimbursements, drainage improvements, and a temporary use of right-of-way fee waiver. The projects have thus far received approximately $710,000 of these incentives. Additionally, the developers have entered into an agreement with Austin Energy for the provision of a chilled water facility valued at approximately $3.5 Million.

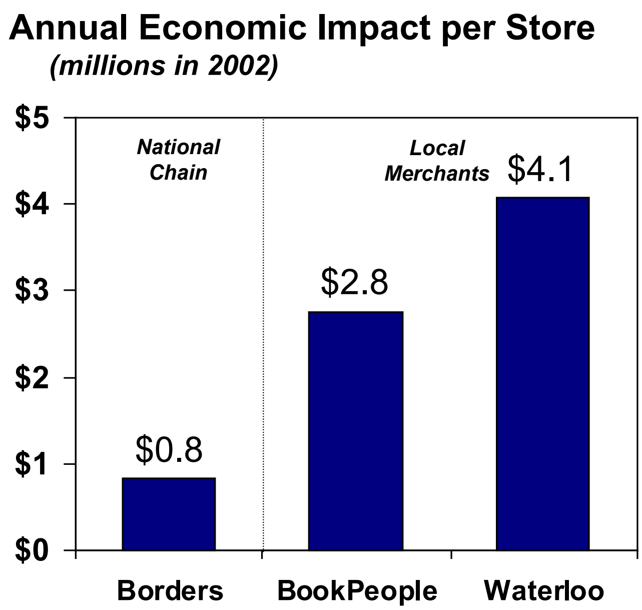
EXECUTIVE SUMMARY

Civic Economics (CivEc) is pleased to present this Economic Impact Analysis assessing the economic activity generated by local merchants relative to a chain merchant carrying comparable lines of goods. Economic impact, for the purposes of this case study, is based on locally focused expenditures of the merchants, including such items as labor, profits, goods, and services.

PRINCIPAL FINDINGS: THREE ESSENTIAL FACTS

FACT: Local merchants generate substantially greater economic impact than chain retailers.

CivEc initially compared the local economic impact of three freestanding stores, a typical Borders, and the existing and known quantities of BookPeople and Waterloo.



Three distinctions account for the dramatic difference seen in the chart at right:

1. Local merchants spend a much larger portion of total revenue on local labor to run the enterprise and sell the merchandise.
2. Local merchants keep their modest profits in the local economy.
3. Local merchants provide strong support for local artists and authors, creating further local economic impact.

FACT: Development of urban sites with directly competitive chain merchants will reduce the overall vigor of the local economy.

Development of a Borders store at Sixth and Lamar will reduce the vigor of the Austin economy. In this analysis, CivEc reviewed three scenarios to account for the range of impacts possible. In all three, Borders triggers a decline in local economic activity despite increasing total sales of books and music at the corner.

Competitive Effects:
Borders Impact over Five Years

Total book and music sales **increase**

Economic returns **decrease**

CivEc puts forth two alternative outcomes in which the neighborhood and the Austin economy will be enhanced:

1. New merchants bring a new line of goods to the market, attracting additional consumer traffic to the area to the benefit of neighboring merchants. For example, former plans called for a cinema at the site. This would have offered a product previously unavailable at Sixth and Lamar, drawing additional prospective customers for all neighboring merchants.

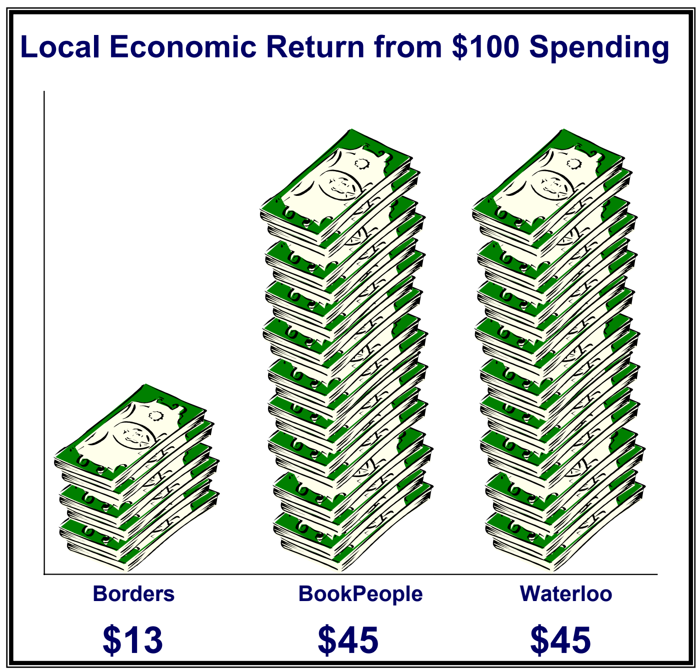
2. New merchants bring a complementary line of goods to the market, leading to increased browsing among merchants with similar but unique lines of goods. For example, there exists in the neighborhood a cluster of antiques and home goods shops. Shoppers for these goods are induced to visit several merchants, as unique yet related items are offered in each shop.

As presently configured, the City of Austin is asked to subsidize a development that actually does damage to the local economy.

FACT: Modest changes in consumer spending habits can generate substantial local economic impact.

For every $100 in consumer spending at Borders, the total local economic impact is only $13. The same amount spent with a local merchant yields more than three times the local economic impact.

If each household in Travis County simply redirected just $100 of planned holiday spending from chain stores to locally owned merchants, the local economic impact would reach approximately $10 Million.



ECONOMIC IMPACT ANALYSIS: LOCAL MERCHANTS vs. CHAIN RETAILERS

This report is divided into three sections, which present similar data in different formats for different audiences.

SECTION I: COMPARATIVE ECONOMIC IMPACT ANALYSIS presents a baseline assessment of the economic impacts of three different, freestanding stores: BookPeople, Waterloo, and a typical Borders. It provides much of the underlying data for subsequent analysis.

SECTION II: COMPETITIVE EFFECTS ANALYSIS is aimed squarely at policymakers. It provides a five-year forecast of the likely effect of competition at Sixth and Lamar.

SECTION III: PROPORTIONATE ECONOMIC IMPACT ANALYSIS is aimed squarely at consumers. It provides shoppers with an understanding of the implications of our purchasing decisions.

Civic Economics has withheld a small amount of the underlying data in order to protect the privacy and business practices of the local merchants in question. Questions regarding methodology and findings should be directed to:

Dan Houston, Partner
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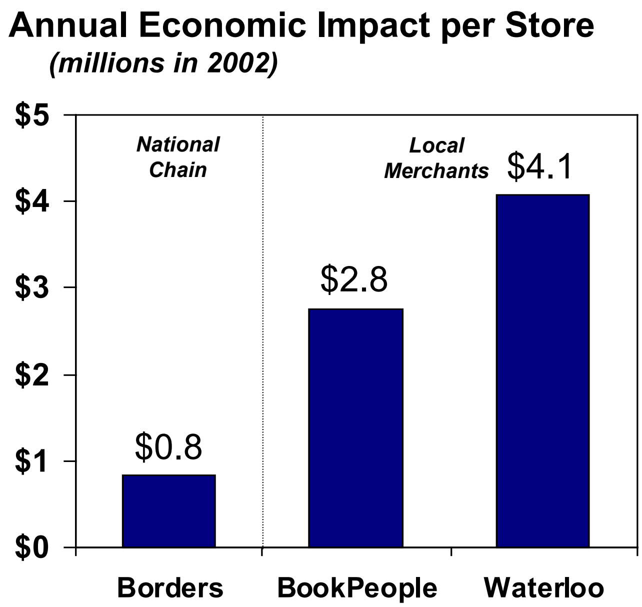
SECTION I: COMPARATIVE ECONOMIC IMPACT ANALYSIS

Locally owned and operated merchants generally have greater impacts on local economies than outlets of national change due to three primary classes of expenditure.



First, spending on **local labor** typically comprises a greater share of operating costs for a locally owned establishment than an outlet of a national chain. While the latter is able to consolidate the vast majority of its administrative functions, such as bookkeeping and advertising, at its national headquarters, an independently owned store carries out those functions in the community. Additionally, "economies of scale" and carefully engineered store layouts may allow national chains to employ fewer sales staff than locally based stores.

Next, large national chains purchase fewer **goods and services** in the markets they serve. Their products, advertising, and supplies are usually procured at the national level. By contrast, local stores may purchase a substantial portion of these goods and services from other local firms, keeping that money in the community. Additionally, local bookstores and record stores are often the sole outlets for retail sales of books and recordings by local authors and artists. Particularly for authors and artists with self-published works, such as local bands selling music on consignment, the bulk of sales receipts remain local. National chain stores stock few such items.

Finally, a larger portion of **profits** earned by owners of local stores remains in the local economy. Once a purchase is made at a nationally owned store, the profits from that sale go directly to the headquarters outside the region, perhaps to be distributed to stockholders worldwide. The owners of local establishments, by contrast, are members of the local community, residing in nearby neighborhoods and spending their earnings on goods and services locally or supporting local organizations.

Chart 1 presents the first standard dataset of an economic impact assessment, the combined direct and indirect economic impacts of each store. In this analysis, CivEc reviewed the local employment and spending patterns of each merchant, using actual data from BookPeople and Waterloo, and a typical Borders store, all in 2002. Details of the underlying data, assumptions, and methodology have been withheld to protect the privacy and business practices of the local merchants.

For the purposes of this report, **direct impacts** are identified as all local expenditures by the store. For example, wages and benefits paid to employees remain local, as does local advertising spending, purchases from local suppliers, and, in the case of the local merchants, profit. By including off-site expenditures as part of the direct impact, this analysis is able to incorporate the marked difference between these purchases made by local establishments and national franchises. In a simple economic impact analysis, off-site expenditures are viewed as indirect impacts, to be estimated by the application of multipliers. However, in this case, such a treatment would yield inaccurate results by estimating that local merchants and chain outlets purchase equal shares of goods and services locally.

Calculation of **indirect impacts** seeks to quantify the further effects of direct impact funds as they circulate in the local economy. Indirect impacts are calculated using **multipliers**, which estimate the degree of circulation expected. The cost of goods for each store, which includes wholesale purchases of merchandise and the space in which to sell it, are not included in the calculations. These indirect impacts also include **induced effects**, accounting for increased household spending brought about by additional local economic activity.

CivEc here utilized conservative, industry standard multipliers, calculated by a nationally respected firm using a sophisticated input-output model of the Austin economy. To protect the privacy and business practices, the precise values of those multipliers cannot be provided in the published version of this report.

Our analysis reveals that the typical Borders store generates total local economic impact of just over $820,000.

By contrast, BookPeople generates total a local economic impact of $2.8 Million.

Similarly, Waterloo generates local economic impact of $4.1 Million.

It must be noted that this is a net economic impact and not a fiscal analysis. This local impact does not seek to determine the amount of revenue each will deliver to the local governmental units involved. Such tax revenue will be similar whether new retailers at the site are a competitive threat to other independent businesses nearby or not.

SECTION II: COMPETITIVE EFFECTS ANALYSIS

Underlying Assumptions

> **Competitive Effects:**
>
> Borders introduces no new products to the market, either at the corner or in Austin.
>
> Approximately 50% of revenue at a new Borders will be diverted from BookPeople and Waterloo.

The analysis described above calculates the economic impact of the three stores in the present year. However, to address the situation at Sixth and Lamar requires consideration of the effect of direct competition at the corner. CivEc has, therefore, formulated a set of assumptions about the performance of these stores in the future and in competition. For the purposes of this study, 2004 has been treated as year one of competition.

Assumption 1: According to recent annual reports of Borders Group Inc., the average Borders nationwide will achieve sales of approximately $6.5 Million in 2002. However, given the expected intensity of competition in comparable merchandise at Sixth and Lamar, we do not believe that this Borders store will perform as well. We have thus assumed a Borders store with first year revenues of $4.7 Million. It should be noted that Borders Stores closed only one outlet in 2001, indicating a willingness to maintain under performing stores for sustained periods. Additionally, our analysis demonstrates that should Borders perform substantially better than projected here, local merchants BookPeople and Waterloo would face extreme challenges to remaining in business.

Assumption 2: The calculation begins with projected revenues for BookPeople and Waterloo, provided by the merchants themselves. In the absence of a Borders at the corner, both project modest annual increases over the coming years. To validate these assumptions, CivEc studied recent retail sales trends (books, music, and overall retail sales) for a large area of central Austin. Books, music, and general retail all sustained strong gains over the last ten years, with a modest decline in 2001. Based upon 2002 sales figures for BookPeople and Waterloo, continuation of modest annual gains is a reasonable assumption.

Assumption 3: CivEc again studied retail sales trends for the region to estimate the likely effect of competition among the stores. Given the similar product mix and nearly identical pricing of those goods, we assumed that approximately 50% of Borders sales at this location would represent sales diverted from BookPeople and Waterloo. This assumption is supported by historical retail data showing consistent but modest increases in book and music sales locally. Given Borders' emphasis on books and the duplication of inventory at BookPeople, we assumed that diverted sales would weigh more heavily on BookPeople than on Waterloo. As to the other 50% of sales, that revenue is likely to be drawn primarily from other merchants throughout the metropolitan area, though a new Borders location may be expected to induce a very small amount of new book and music spending in the region.

Assumption 4: Finally, CivEc formulated three likely outcomes in succeeding years. In the first, labeled the Basic Borders, the Borders store is projected to gain revenues at an annual rate of 2%, in line with both the industry overall and with the chain's same-store sales in recent years. In the second, labeled the Weak Borders case, Borders is projected to lose revenues at an annual rate of 3% as local competitors retake lost market share. In the third, labeled the Strong Borders case, Borders is projected to consolidate its position and gain revenues at an annual rate of 7%. For the local merchants, we also include a No Borders scenario, using the projected revenues described in Assumption 2.

All charts in the remainder of Section 1 incorporate variations on these assumptions and scenarios. As with other analyses in this report, details of revenue forecasts are withheld to protect the privacy and business practices of BookPeople and Waterloo.

Competitive Effects Scenarios

The following charts illustrate the range of competitive effects for Borders, BookPeople, and Waterloo.

Borders sales are forecast to begin at $4.7 Million, and rise to nearly $5.1 Million in the Base Case, with high and low projections of $6.1 Million and $4.1 Million by 2008.

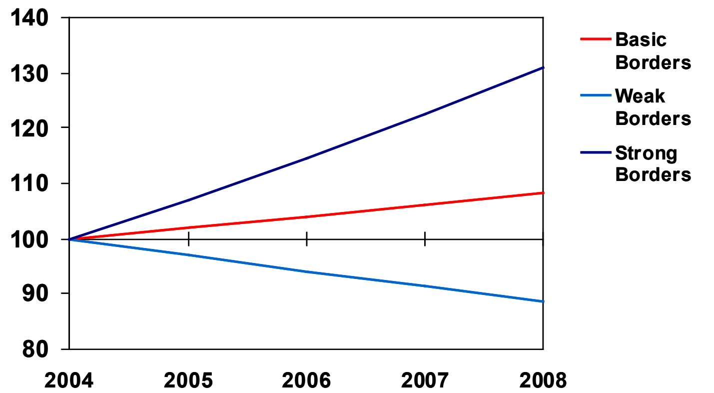
In these projections, sales diverted from BookPeople and Waterloo will be expected to total between $11 Million and $14 Million over the course of five years.

At first glance, these projections might appear extreme. However, the present situation is particularly clear. This study involves merchants selling very similar lines of goods at nearly identical prices so the competition will be intense.

We have no doubt that the first year of competition at the corner will produce profound changes in revenue for BookPeople and Waterloo. Moving forward, similarly strong effects will be felt as competition settles into a pattern.

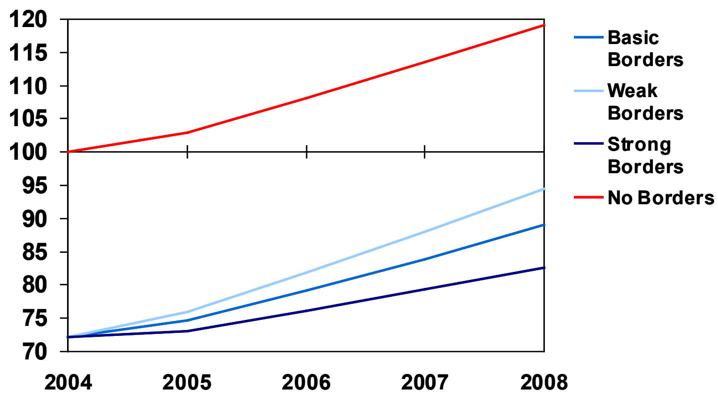
Borders Sales Forecast, '04 to '08

(Indexed: 2004 Sales = 100)



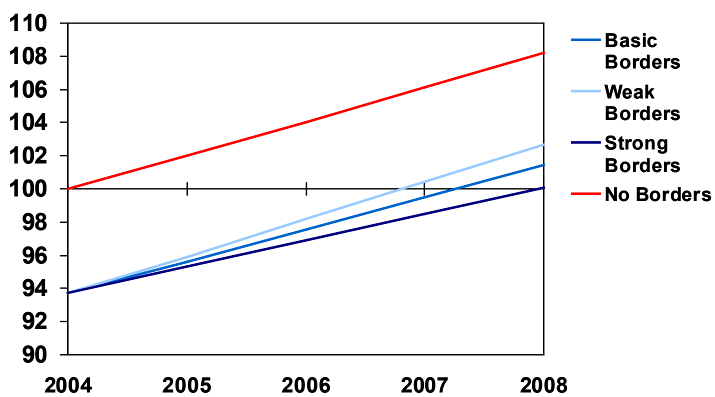
BookPeople Sales Forecast, '04 to '08

(Indexed: 2004 Sales = 100)



Waterloo Sales Forecast, '04 to '08

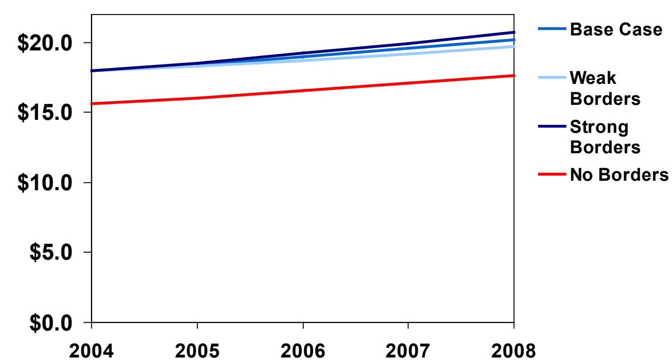
(Indexed: 2004 Sales = 100)



Economic Impact of Competition

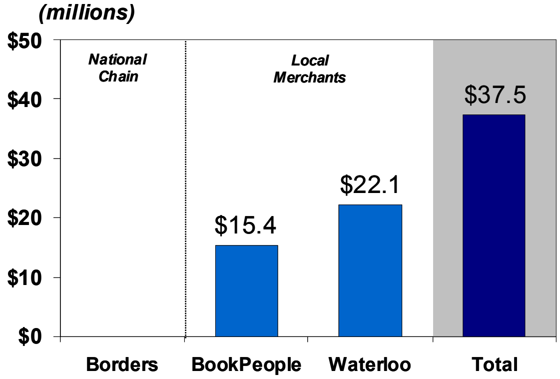
At first glance, citizens and policymakers might view the scenarios above as the result of healthy competition, enhancing consumer choice and value. Indeed, in such a dynamic marketplace as Austin, such shifts are taking place every day in every line of merchandise. In all of the scenarios, total sales of books and music (and therefore total sales tax revenue) at the intersection will increase.

Total Sales Forecast, Books & Music, '04 to '08
(millions)

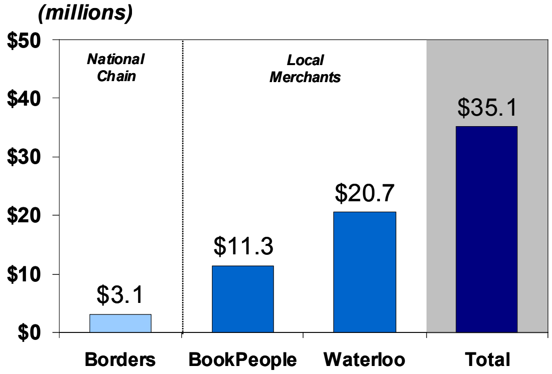


However, the total return to the community entails activity beyond retail sales and sales tax collections at a given location. The economic health of the city is impacted as well by wages paid to local residents, by materials and supplies purchased locally, and by the reinvestment of profits in the business and in the community. These factors are the building blocks of economic impact.

Cumulative Gross Impact without Borders, '04 thru '08
(millions)



Cumulative Gross Impact with Base Case Borders, '04 thru '08
(millions)



CivEc undertook to analyze the economic impact on the local economy of each of these scenarios. In making these calculations, we assumed that all merchants would increase or reduce expenses in proportion to changed revenue. In the Strong Borders scenario, for example, Waterloo will be expected to experience a decline in revenue of 7%. Therefore, the analysis incorporates a 7% reduction in expenditures for labor, materials, and services purchased locally.

In every scenario above, despite additional total sales, **the total economic activity generated by these merchants is projected to decline after the opening of a Borders and Sixth and Lamar**.

This counterintuitive outcome occurs because every dollar drawn away from a locally owned merchant by a chain store results in a net loss to the local economy. Activity generated by new sales does not replace the activity lost in that diversion of sales.

Policy Implications

Policymakers often feel compelled to draw chain retailers into a jurisdiction as a means of increasing sales tax collections, an apparently painless way of maintaining necessary government services without resorting to tax increases. If we look only at the corner of Sixth and Lamar, sales tax collections will indeed increase if a Borders opens. That is true, however, regardless of what opens on that site.

Alternative Outcomes:

- ➢New merchants bring a new line of goods to the market
- ➢New merchants bring a complementary line of goods to the market
- ➢New merchants contribute to local economic vitality

In the case at hand, increasing sales tax revenues by siting a chain store directly across from local merchants selling similar goods at similar prices actually results in reduced economic activity.

This analysis clearly demonstrates that public goals will be better served by promoting alternative retail options at the corner.

Two scenarios present more desirable outcomes:

1. New merchants bring a new line of goods to the market, attracting additional consumer traffic to the area to the benefit of neighboring merchants. For example, former plans called for a cinema at the site. This would have offered a product previously unavailable at Sixth and Lamar, drawing additional prospective customers for all neighboring merchants.

2. New merchants bring a complementary line of goods to the market, leading to increased browsing among merchants with similar but unique lines of goods. For example, there exists in the neighborhood a cluster of antiques and home goods shops. Shoppers for these goods are induced to visit several merchants, as unique yet related items are offered in each shop.

A policy preference for local merchants will produce even greater economic vitality.

Current smart growth policy and downtown development programs have created the in this situation the unfortunate side effect of offering financial and development assistance to a project that will actually sap economic vitality from the urban core.

SECTION III: PROPORTIONATE ECONOMIC IMPACT

The economic impact analysis above provides compelling evidence of the public benefits of local merchants relative to chain retailers. How might consumers use this information to modify spending habits? The following analysis identifies the relative value provided to consumers and the economic impact of their spending.

Value to Consumers

Value to Consumers:

Prices for books and music are nearly equal at Borders, BookPeople, and Waterloo.

30% of comparison shopping selections were not in stock at Borders.

CivEc, with BookPeople and Waterloo staff, prepared shopping lists for comparison. These selections were not made in a scientific manner, merchants were simply instructed to identify five titles in each of five categories of books or music. They did not engage in comparison shopping before making these lists. CivEc then undertook to compare the availability and cost of these items at each store.

In the case of books, it is clear that Borders is not a "discount store." In this atypical industry, prices are printed on the product at the factory, and both BookPeople and Borders use those prices in nearly every case. Every item on the shopping list was priced the same at both merchants. Moreover, approximately 30% of these items were out of stock at the Borders store used for comparison.

In the case of recorded music, comparison shopping proves more difficult. Austin's Waterloo Records is among the top performing independent record stores in the nation, and stocks an extraordinary variety of titles, from the latest popular music to the most obscure local bands. For those titles on the shopping list that were in stock in both places, aggregated prices were essentially equal, though price advantages among titles varied considerably. In an independent comparison-shopping exercise, the Austin American-Statesman recently found a savings of 8.5% at Waterloo versus Borders. ("At What Price Music," Austin American-Statesman, December 5, 2002).

Consumers seeking the most popular titles and artists receive equal value at each of the three merchants studied. However, the consumer whose tastes run to more esoteric books or local music is far better served at BookPeople and Waterloo. Indeed, these findings emphasize the homogenizing effect of chain retailers. The consumer who shops only at Borders may remain unaware of many artists and authors outside the mainstream of the publishing and recording industries.

Local Impact

Having established comparable value and better selection, CivEc then calculated the local economic impact of $100 in consumer spending at each of the three stores.

When the consumer spends $100 at Borders, approximately $9 remains in Austin, primarily in the form of employee salaries. The remainder is transferred out of the city almost immediately, in the form of wholesale expenses, administrative costs incurred elsewhere, and profits. Applying industry standard multipliers to calculate total economic impacts, this $100 spent yields a total of $13 in local economic impact.

By contrast, consider that same $100 spent at BookPeople or Waterloo. There, as much as $30 is directly injected into the local economy. Again, much of this is kept local in the form of employee salaries, but with local merchants administrative expenses and profits are also directly placed into the Austin economy. Applying the same multipliers to calculate total economic impacts, this $100 spent yields a total of over $45 in local economic impact.

Consider this: If each household in Travis County redirected just $100 in holiday spending, the local economic impact of that simple act would reach approximately $10 Million.

ABOUT THE PROJECT PARTICIPANTS

LiveableCity Austin is an inclusive network of individuals working together to create a community consensus to promote policies that address the long term social, environmental and economic needs of the people of Austin.

Civic Economics (CivEc) is an economic analysis and strategic planning consultancy with offices in Austin and Chicago.

BookPeople and Waterloo Records and Video provided additional funding and research support for this study, with support from the Austin Independent Business Alliance.

For further information about the project participants or this Economic Impact Assessment, please contact:

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Big Box Retail And Austin: An Independent Review

Prepared for:

Austin Independent Business Alliance
Austin Full Circle
Liveable City
AFSCME Local 1624

October 6, 2004

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EXECUTIVE SUMMARY

On June 24, 2004, the Austin City Council (COA) received a long-awaited study, *Big Box Retail and Austin*[1], prepared by Texas Perspectives (TXP) and the Gateway Planning Group. This study was intended to assess the economic impacts of increased big box development in Austin and was to address seven key tasks assigned by City Council. Three Austin civic organizations (the Austin Independent Business Alliance, Austin Full Circle, and Liveable City) became concerned that the report provided insufficient and/or inaccurate guidance to the Council. In response, they asked three nationally known authorities to review *Big Box Retail and Austin* and provide independent analysis of the report, its methodology, and its conclusions.

While the COA study contains extensive and valuable information, the reviewers are troubled by its essential findings. Our principal concerns are as follows:

- We strongly question the study's central conclusion that the city's principal concern should be establishing design standards for a subset of big box retailers. Design standards alone cannot address economic impacts. Managing and mitigating the economic impacts of big box activity will require appropriate market based solutions that account for the full costs and benefits of big box development.

- Evidence presented in the study is insufficient to support the claim that "there appears to be relatively little direct competition between big boxes and local retailers." Most evidence in fact suggests that a rapid increase in big box retail *does* take business away from many types of local retail.

- The study does not provide any specific measures of the public health, public safety, traffic, and infrastructure costs of big box development. These measures are crucial to assess the true costs of big box development for the City.

- Studies conducted elsewhere show that the low-wage/low-cost strategy employed by many big box retailers generates specific costs for local governments and taxpayers (e.g. indigent health care, affordable housing and public safety). In effect, host communities must subsidize wage and service costs for large, highly profitable corporations.

- The 21.2% big box retail market share cited by the authors is a misleadingly low figure, shaped by the authors' somewhat arbitrary definition of big box, which limits their inquiry to six specific retailers. A more accepted definition, such as the one formulated by Columbia

[1] The complete text of *Big Box Retail and Austin* is available for download at: *www.ci.austin.tx.us/redevelopment/downloads/Big%20Box.Austin.final.pdf*

University and cited by the authors, would reveal that big boxes already control a much larger market share in Austin.

- Inaccurate regional retail sales estimates released in the original report paint a false picture of suburban retail drain. In fact, Austin continues to significantly outperform suburban jurisdictions for retail sales.

- A viable strategy for Austin would include policies to support unique local retail establishments, while guiding the placement, and in some cases limiting the size of big boxes.

This review is not, however, entirely critical. Rather, we have sought to provide additional guidance to the City Council in formulating consistent and effective policies regarding big box development in the City of Austin.

We believe the following recommendations provide a roadmap for future policy consideration:

1. Require a Conditional Use Permit for all proposed large-scale retail developments including an impact analysis to demonstrate net benefits and costs to the community, with the possibility of negotiated exactions to mitigate the true costs of the development not offset by tax contributions. Based on the model recently adopted by Los Angeles, such an analysis might include financial impacts, employee impacts, design standards, and reuse provisions to prevent abandoned big boxes.

2. Develop long-term strategies to strengthen and enhance our local retail market. To this end, we strongly recommend future actions in four key areas.

    - Regarding major employers, the City should incentivize only those who pay wages and benefits that allow employees to be self-sufficient.
    - Develop policies that strongly support local independent businesses.
    - Identify the current market share of *all* big box retailers in Austin, not limited to the six specific retailers in the current study, with the goal of establishing a diverse retail balance to sustain a healthy, competitive, market.
    - Explore a regional compact as a means to ameliorate tax incentive competition among area jurisdictions to capture retail activity.

It is important for city leaders to be aware that communities across the U.S. have taken action to manage the development of big box retail. It is widely recognized that big box development generates external costs that cities must address to ensure balanced retail development and benefits that at least equal the costs to municipalities. The Conditional Use Permit called for here is not unreasonably burdensome, but necessary to ensure a vibrant retail economy.

This document provides an independent review of *Big Box Retail and Austin*, which was presented to the Austin City Council on June 24, 2004.

This review was prepared by the following individuals:

- **Dan Houston**, a partner in Civic Economics, an economic analysis and strategic planning consultancy with offices in Austin and Chicago.
  www.CivicEconomics.com

- **Michael Oden**, Associate Professor of Community and Regional Planning in the School of Architecture at the University of Texas at Austin.
  wnt.utexas.edu/architecture/people/faculty/odenf.html

- **Bill Spelman**, Professor of Public Affairs in the Lyndon Baines Johnson School of Public Affairs at the University of Texas at Austin.
  www.utexas.edu/lbj/faculty/spelman.html

This review has been organized and endorsed by the following civic organizations:

- **Austin Independent Business Alliance**, representing the interests of over 300 locally owned businesses in the Austin area.
  www.Austin-IBA.org

- **Austin Full Circle**, an all-volunteer coalition of business, labor, environmental, and neighborhood leaders focused on corporate responsibility and the economic impacts of increased big box development.
  www.AustinFullCircle.org

- **Liveable City**, an inclusive network of individuals working together to create a community consensus to promote policies that address the long-term social, environmental, and economic needs of the people of Austin.
  www.LiveableCity.org

- **AFSCME Local 1624**, a local union representing employees of the City of Austin and Travis County and an advocate for sustainable wages and benefits for working people throughout the community.
  www.AFSCME1624.org

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BIG BOX RETAIL AND AUSTIN: AN INDEPENDENT REVIEW

Background

In recent years, Austin City Council has been faced with numerous issues related to what is known as big box retail. In each case, Council was presented with unique circumstances and sought to craft appropriate solutions. These solutions were of necessity developed on an ad hoc basis; environmental protection, economic development, and neighborhood planning considerations had to be balanced in each case.

Council wisely recognized the need for further information in order to develop a consistent policy framework for dealing with big box retail. In November 2003, the Austin City Council commissioned a study of the impact of "big box retail" to be prepared by Texas Perspectives (TXP) and the Gateway Planning Group (Gateway), a move that was supported by three Austin civic organizations (the Austin Independent Business Alliance, Austin Full Circle, and Liveable City). These respected consultants were asked to report to the Council on the economic, environmental, fiscal, and social impacts of “big box retail,” a term left undefined in the commission.

Specifically the report was to address seven tasks delineated by the City:

1. Outline recent trends in retailing nationwide;
2. Provide an overview of the status and history of retail trade in Austin and the greater Austin area;
3. Review the academic and trade literature related to the impact of big boxes and national brand retailers on local economies;
4. Survey the Austin market to determine prices for certain goods from national brand retailers, regional providers, and small locally-owned businesses;
5. Survey national brand retailers, regional providers, and small locally-owned businesses to determine the range and scope of both labor compensation and local procurement;
6. Assess crime and traffic counts to determine relative impacts on public safety and the environment;
7. Integrate the above findings with available information on “best practices” regarding public policy on land use related to retail to make policy recommendations.

On June 24, 2004, Jon Hockenyos of TXP presented the report, *Big Box Retail and Austin*, to City Council. The Austin Independent Business Alliance, Austin Full Circle, and Liveable City became concerned that the report provided insufficient and/or inaccurate guidance to the Council. In response, they asked the three of us to review *Big Box Retail and Austin* and provide an independent analysis of the report, its methodology, and its conclusions. This document is the result of our analysis.

The authors of this review have great respect for the work of TXP and Gateway. Moreover, we recognize the daunting scope of the charge to assess the impact of big box retail. Nonetheless, we share strong concerns about the report and the guidance it provides to a Council facing important policy issues. In the following pages, we have highlighted these concerns. Some of these deal with methodology and execution and are necessarily technical. Others deal with findings and implications and are necessarily subjective. This document, admittedly, raises as many questions as it answers; the authors worked on this evaluation on a voluntary basis and could not devote resources to conduct a complete re-analysis of the entire scope of work.

Specifically, we strongly question the central conclusion of *Big Box Retail and Austin* that the principal concern of city government should be in establishing design standards for a subset of big box establishments. Design standards alone cannot address economic impacts.

As studies and actions in numerous communities across the country demonstrate, the impacts of rapidly evolving big box retail on local conditions are serious and pervasive. Managing and mitigating these impacts requires appropriate market-based solutions that go beyond simple design standards.

We have organized this review into seven sections, corresponding to the seven tasks assigned by the City Council at the outset of the study.

TASK 1: OUTLINE RECENT TRENDS IN RETAILING NATIONWIDE.

Defining Big Box Retail

Big Box Retail and Austin provides a solid discussion of the variety of retailers that might be labeled "big box." These retailers are distinguished from one another in two ways. The first is the retail strategy of each merchant. The second is the nature and size of the building itself, whether freestanding or attached.

These distinctions are important for different reasons. The retail strategy of a merchant presents *economic and social issues* for consideration. The site and nature of the building, on the other hand, presents *planning, environmental and design issues.*

In this case, six merchants were identified for further evaluation. Four of them (Wal-Mart, Target, Sam's, and Costco) are easily recognized as big box retailers. They offer an enormous variety of merchandise and do so in massive, freestanding stores.

Two additional merchants identified for further evaluation (Home Depot and Lowe's) are substantively different from the general merchandisers above. These stores are essentially category killers, focusing on a particular range of goods under the rubric of home improvement. Like the general merchandisers above, Home Depot and Lowe's operate massive, freestanding stores. However, their retail strategies are more analogous to other category killers such as Best Buy and Fry's in electronics, both of which are widely recognized as big box retailers.

In our view, the particular selection of these specific retailers (a mix of general merchandisers and category killers) is somewhat arbitrary and in many ways shapes the conclusion of the study. Why the authors chose a 100,000 square-foot cutoff and excluded other category killer big boxes such as Barnes and Noble, Frye's, Circuit City, Toys "R' Us, Office Depot, etc., is unclear. Other, more common definitions - such as the Columbia University definition first cited by the authors - could lead to different conclusions.

In particular, the definition in *Big Box Retail and Austin* muddies the distinction between economic and design considerations. Having effectively selected a subset of large national merchants based on size and building design, the study unsurprisingly focuses on design solutions, relegating economic considerations to secondary status.

Big Box Competitive Strategies and Property "Churning"

There is an additional characteristic of national big box retail not fully addressed in the study. As the authors convey in their overview of the retail market, in areas where big box establishments are concentrated, retailers face fierce competition, resulting in a lot of "churning" or rapid turnover of firms and properties. Competition from tax-advantaged internet retailers is also pinching these markets. As Wal-Mart, Target, Circuit City, and Home Depot expand, K-Mart, Best Products, J.C. Penney, and Wards radically downsize or close all store locations.

In addition, successful big box retailers often abandon older, smaller stores for bigger sites or shift to new locations. The short residency of many big box retailers in specific sites leaves large vacant buildings that sometimes trigger more extensive commercial vacancy and blight in specific commercial areas. According to Wal-Mart's own website (www.wal-martrealty.com), the chain now has roughly 400 vacant stores available nationwide, including 42 in Texas and two in Austin.

A recent report by the City Attorney's Office of Los Angeles emphasizes the potentially negative impacts associated with the practice of big box superstores negotiating leases that permit them to vacate a location, while maintaining the lease on the stores and parking.

> [This practice] "facilitates a pattern of superstores locating in a community, engaging in predatory pricing that drives out competitors, consolidating their operations by shutting down stores once competition is eliminated and then tying up the massive parcels they have assembled through long-term leases that prevent the reestablishment of rival retailers and the recycling of industrial and commercial property. This ultimately results in declining property values for the surrounding community as a hulking vacant structure sits on an enormous parcel attracting graffiti and debris.[2]"

A study of the Kansas City market found that big boxes (defined in that study as a retail store of 25,000 square feet or more) accounted for 56.8 percent of the total vacant commercial property in the Kansas City area in 2000[3]. This pattern of property churning, characteristic of big box development, points toward the need for a special ordinance ensuring that vacated property be maintained by the developer or tenant and that vacant property is promptly put on the market. At the same time, the city might explore ways to guide new big box development or other uses to pre-existing vacated properties instead of greenfield sites.

[2] City Attorney's Office of Los Angeles, "Options for Regulating the Development of Superstores," Report No. R03-0585, Dec 2003, page 5.
[3] R.H Johnson Company, *Metropolitan Kansas City: Year 2000 Shopping Center Report.* Kansas City, Missouri, 2000.

TASK 2: PROVIDE AN OVERVIEW OF THE STATUS AND HISTORY OF RETAIL TRADE IN AUSTIN AND THE GREATER AUSTIN AREA.

Movement of Spending to the Suburbs

Big Box Retail and Austin makes an effort to identify the share of the regional retail market captured within the City of Austin over time. However, the printed report released to the Austin *American-Statesman* made a serious error in calculating these shares[4].

In the original calculations, TXP estimated that Austin's share of regional retail activity had fallen from 83.5% to 53.9% from 1990 to 2003, indicating a precipitous trend in which Austin's retail share may soon fall below its population share. Prompted by the authors of this Review, TXP corrected these figures, yet left the conclusions unchanged.

Austin Metropolitan Area Retail Sales History

	Sales Tax Allocations (Millions)		Tax Rates		Retail Sales (Millions)	
	2003	1990	2003	1990	2003	1990
Austin	$105.10	$48.40	0.0100	0.0100	$10,510.00	$4,840.00
Bastrop	$2.50	$0.40	0.0150	0.0100	$166.67	$40.00
Bee Cave	$1.60	$0.10	0.0200	0.0150	$80.00	$6.67
Cedar Park	$6.80	$0.40	0.0200	0.0100	$340.00	$40.00
Georgetown	$5.90	$0.90	0.0175	0.0100	$337.14	$90.00
Lakeway	$0.90	$0.10	0.0125	0.0100	$72.00	$10.00
Leander	$0.50	$0.10	0.0100	0.0100	$50.00	$10.00
Pflugerville	$1.80	$0.10	0.0150	0.0100	$120.00	$10.00
Round Rock	$46.10	$2.90	0.0200	0.0150	$2,305.00	$193.33
San Marcos	$12.50	$3.00	0.0150	0.0150	$833.33	$200.00
Sunset Valley	$3.80	$0.00	0.0175	0.0100	$217.14	$0.00
Taylor	$2.10	$0.60	0.0200	0.0100	$105.00	$60.00
West Lake Hills	$1.60	$0.30	0.0150	0.0100	$106.67	$30.00
MSA Municipal Total	$194.90	$58.00			$15,242.95	$5,530.00
Austin Share	53.90%	83.50%			69%	88%

	2003	1990
Austin Pop. Share	50.0%	55.8%
Austin Sales Share	69.0%	88.0%

Source: Texas Comptroller

[4] In Table 6 of the draft circulated prior to release, “Sales Tax Allocations” were treated as a proxy for retail sales in each municipality. However, a further calculation is required to adjust for the differing sales tax rate in each municipality. In fact, because Austin has the lowest municipal sales tax rate among those studied, the city share of total retail sales was substantially undercounted.

When the figures for retail market shares are corrected for actual retail sales, it becomes clear that Austin continues to outperform suburban jurisdictions by a substantial margin. In 1990, Austin's share of metropolitan population stood at 56%, yet city stores accounted for 88% of regional retail sales. By 2003, city population was at approximately 50% while city stores still accounted for 69% of all retail sales in the metropolitan area. Even today, as Austin's suburbs continue to expand in both population and business activity, the City of Austin captures retail activity far exceeding its share of regional population.

As the Austin MSA continues to grow, the retail and population shares of the City will likely see some convergence in future decades. However, *Big Box Retail and Austin* paints a misleadingly dire picture of suburban retail flight, exaggerating decline and pointing to very different policy concerns than a more accurate calculation. Indeed, rather than creating a sense of desperation to remain competitive, the corrected figures should lead to a discussion of why urban retail is so vibrant in Austin and how those advantages might be supported and further developed.

Big Box Retail and Austin forecasts that Austin will likely drift downward until reaching "a market share that is more closely aligned with the central city's share of regional population." We do not believe that resignation to suburban-style retail is the proper response to the data. On the contrary, we believe these figures highlight the city's substantial advantages as a retail destination. The mixed use, pedestrian friendly, and "weird" retail offerings in Austin cannot be duplicated in the suburbs and should instead be nurtured and protected in order to preserve the city's share of urban retail activity and sales tax generation.

TASK 3: REVIEW THE ACADEMIC AND TRADE LITERATURE RELATED TO THE IMPACT OF BIG BOXES AND NATIONAL BRAND RETAILERS ON LOCAL ECONOMIES.

Background

It is important to recognize that retail activity is generally the result, rather than the cause, of economic growth in a city or region. Retail is basically dependent upon the condition of the local economy, especially core regional export industries. *Retail activity cannot grow more rapidly than disposable income within a given regional economy.* To the extent that new or expanding retail establishments grow faster than local purchasing power, there is competition and some crowding out. Some new activity displaces sales at existing establishments – retail big box expansion can crowd out sales from local merchants or other national chains already in place. The job, sales and tax gains from a given big box project cannot be viewed as net gains to a community.

This is also why it makes little economic sense to offer public incentives to retail. Retail incentives often simply shift economic activity from one place to another rather than generating new products and jobs. Unfortunately, many communities try to capture retail activity from neighboring jurisdictions in an attempt to secure new tax revenue. In most cases, these strategies, sometimes called "beggar thy neighbor," lead to a net loss in social welfare for citizens of a region. Sensible regional compacts to limit retail tax giveaways could do much to ameliorate these negative impacts.

Economic Impact of Big Box Retail on Local Merchants

In Finding #2 of their report, the authors state: "There appears to be relatively little direct competition between big boxes and local retailers; where competition exists, prices tend to be comparable." This bold conclusion is essentially based on three pieces of evidence:

- Literature that suggests that local merchants can most effectively compete with big boxes by offering something different;
- A limited survey of national big box, regional big box (e.g. HEB, Academy), and a few local retailers in six product categories;
- An analysis of the Austin retail market share limited to six companies defined by the authors as national big boxes.

In each case, evidence offered in the study is not sufficient to support the "relatively little direct competition" conclusion.

Evidence of Significant Direct Competition

The first problem with this bold claim is that it fails a basic reality test. A ten-minute discussion with a local merchant in the book, grocery, hardware, toy, office supply, electronics or sporting goods business would likely reveal that they are under intense competitive pressure from national big box retailers.

Citing Iowa State economist Kenneth Stone, the authors note that local merchants can only survive by offering different products or unique higher-level service to customers. But the central point of Stone's work is that discount mass merchandisers have a devastating effect on local merchants in towns that do not host a big box. To quote from the abstract of one of Stone's papers, "There is strong evidence that rural communities in the United States have been more adversely impacted by the discount mass merchandisers (sometimes referred to as the Wal-Mart phenomenon) that by any other factors in recent times.[5]" Stone replicated his study of rural Iowa communities with eight small- to medium- sized cities (communities of over 50,000). His findings were similar: communities with national mass merchandisers experienced growth in retail sales, but this growth resulted from cannibalizing retail in nearby towns that then experienced a decline in their retail sales.

[5] Stone, Kenneth E., "The Impact of the Wal-Mart Phenomenon on Rural Communities" *Proceedings of Increasing Understanding of Public Problems and Policies-1997*, p. 2.

Jones and Doucette, in a study of the urban market of Toronto found that big box employment in supermarkets, electronics, hardware, toy, sporting goods, books and office products increased significantly between 1993 and 1997, while employment in non-big box formats in the same categories decreased. The Toronto study also surveyed over 18,000 local retail shops and found that their share of local retail sales declined over the same period.[6]

The fact that local retail survivors have moved or been pushed into a new niche or significantly changed their business tactics does not equate with "relatively little direct competition." Indeed, as several commentators have noted, innovative niche and service strategies of smaller retailers are always subject, if successful, to replication by larger national retailers. The authors of *Big Box Retail and Austin* imply this form of competitive vulnerability when they discuss differentiation among big box merchants with some moving into higher quality and service intensive segments.

The product and price comparison survey in the study, while interesting, is far too limited in scope to draw conclusions about competitive conditions across Austin's retail markets. Indeed, the preponderance of existing evidence is consistent with the reality test mentioned above: national big box retailers *do* put significant competitive pressure on local merchants.

The key point is not that local merchants can or should be protected from the competitive pressures of big box retail. However, it is naive to believe that rapid big box development will not have a significant impact on locally owned retailers in many segments. Big box development does not represent a pure windfall in new sales, employment or tax revenue for the city; there will certainly be at least some crowding out of other retail activity. Careful analysis and management of big box development is critical if one believes - as TXP itself previously found in its 2002 white paper, *Austin's Economic Future* - that the unique and durable strength of the Austin retail base is our diverse mix of local establishments.

The Market Share of Big Box Retailers

The report makes a solid effort to estimate the share of the Austin retail market that has been captured by the six retailers selected for study. The methodology is reasonable, developing sales estimates for selected retailers based on corporate average sales per square foot. **However, we are troubled by the finding that "implied big box market share is 21.2%." This market share estimate is totally contingent on how the authors define big box retail, and it should be made very clear that this market share includes only the six merchants studied.** A broader unqualified interpretation of this market share figure has led to confusion not just in the press but in Council chambers, as well.

[6] Jones, Ken and Michael Doucet, "The Impact of Big Box Development on Toronto's Retail Structure," Center for the Study of Commercial Activity, Toronto, 1999.

We believe the same methodology should be applied to additional merchants, particularly the so-called category killers that operate large stores and seek to capture large market share in particular retail sectors. In general terms, the big boxes are large-format stores that typically range in size from 20,000 to over 150,000 square feet. However, the definition of "big" is relative and must be related to the product category in question.

For the supermarket/grocery sector, a big box superstore normally must be in the 50,000 to 100,000 square-foot range. For warehouse operations, such as Costco and Sam's Club, big boxes normally contain 120,000 square feet. In contrast, for book retailers, 25,000 to 50,000 square feet could qualify as a big box operation. For other specialty retail categories, for example, eyeglasses, a 5,000 square-foot store might constitute a "big box."

The key point is that category killer stores are several times the size of a traditional outlet in their category. Therefore, if the study significantly expanded its definition to incorporate even category killers of over 50,000, including such stores as Frye's, Circuit City, and Best Buy, the 21.2% market share calculation would increase substantially.

Another approach would be to look at market shares in specific retail categories. Using only the figures provided in the current study, for example, it is possible to calculate that Home Depot and Lowe's combine for approximately 50% of the total market in building materials. Clearly, where a 20% market share sets off few alarm bells, 50% might generate a very different reaction. These calculations should be done in other retail sectors to identify areas where competition is potentially - or already - impaired.

Home Improvement Competition

	Sales 2003
Home Depot	$492,778,524
Lowes	$194,846,201
BigBox Total	$687,624,725
Building Materials Total	$1,370,000,000
Big Box Share	**50%**

Source: Big Box Retail and Austin, TXP

Differential Indirect Effects of Big Box Versus Local Retail

Big Box Retail and Austin makes a limited effort to evaluate the economic impact of big boxes on local economies. Indeed, it disregards entirely one of the seminal studies in this area. The study[7] conducted by Civic Economics focused on the market for books and music at Sixth and Lamar and has been reviewed and cited around the nation for well over a year[8]. That study documents the

[7] *Economic Impact Analysis: A Case Study of Local Merchants vs. Chain Retailers*, was sponsored by Liveable City, Austin Independent Business Alliance, BookPeople, and Waterloo Records and is available for download at *www.liveablecity.org/lcfullreport.pdf*.
[8] For a partial list of media and organizational citations of the Liveable City Study, see *www.civiceconomics.com/html/retail_network.html*.

substantial economic advantage to those communities with strong locally-owned merchants. *Big Box Retail and Austin* does cite a subsequent study conducted in Maine that replicated these findings using a national big-box retailer for comparison.[9]

The dramatic move on the part of a number of big box retailers to purchase offshore has further diminished the potential local benefit of purchasing by national chains. For example, in 1995, Wal-Mart claimed that only 6% of its merchandise was imported, while by 2003, fully 50-60% of its products came from foreign producers.[10]

Another indirect economic effect deals with the procurement of services in the host community. Professional services such as law, accounting, advertising, and banking are generally provided locally for local merchants. By contrast, national big box retailers generally procure these services in the headquarters community or in the national market.

Studies that show the significant benefits of local retailers to local economies, as opposed to the drain often presented by big box chains, are dismissed in the report as "of limited scope," but we believe they should be part of the discussion in Austin, as they are elsewhere in the nation. If big boxes crowds out local retail activity, then the economic impacts include not only lost sales, but also a loss in indirect activity from re-spending by local merchants on locally produced services and goods.

TASK 4: SURVEY THE AUSTIN MARKET TO DETERMINE PRICES FOR CERTAIN GOODS FROM NATIONAL BRAND RETAILERS, REGIONAL PROVIDERS, AND SMALL, LOCALLY OWNED BUSINESSES.

As noted above, the study did a limited survey of national big boxes, regional big boxes, and a few local merchants, concluding that where competition between big boxes and local retail does exist "prices tend to be comparable." However, the survey is not of adequate scope to draw any meaningful conclusions about competition or product price differentials.

The Market Basket Survey

It appears that TXP attempted a thorough and thoughtful market basket study to assess consumer savings provided by the six selected big box retailers. The study found comparable prices on comparable items between big boxes and local merchants, but often found different grades of goods available. Again, the

[9] "The Economic Impact of Locally Owned Businesses vs. Chains: A Case Study in Midcoast Maine," Institute for Local Self-Reliance and Friends of Midcoast Maine, September 2003. Retrieved from *http://newrules.org/retail/midcoaststudy.pdf*.
[10] Cleeland, Nancy and Evelyn Iritani, "The Wal-Mart Effect: Scouring the Globe to Give Shoppers an $8.63 Polo Shirt," Los Angeles Times, November 24,2003, p. A-1.

finding offered is "little direct competition," but further research suggests a different explanation for the distinction.

Big Box Retail and Austin highlighted two items from the market basket for further discussion, a charcoal grill and a pair of blue jeans. These items, coincidentally, illustrate keenly the nature of the competition between big boxes and local merchants.

The Weber Smokey Joe grill is an American icon, providing the entry-level model for a manufacturer that has built its name on quality. In the market basket study, TXP found that the big boxes carried only the "basic" model, while local merchants offered instead "Silver" and "Gold" versions. A call to the Weber customer service line, however, confirmed that the Silver model (#10020) sold at many retailers is, in fact, the basic model. As part of its purchasing agreement with Weber, Wal-Mart does not market it as "Silver," obscuring the direct competition with other retailers on this item.

Blue jeans are also highlighted as an example of the difficulty in comparison-shopping between local and big box retailers. The recent entry of Levi Strauss into big box discount retail channels has been extensively discussed in the business press. The challenge for Levis was that their longstanding dedication to quality and to American workers was inconsistent with the low-cost strategy of big boxes. To meet the low-cost demands of Wal-Mart, the company created a new line of products, identified as Levis Signature, and outsourced all manufacturing of this line to overseas firms.

Both of these examples, held out in *Big Box Retail and Austin* as confounding direct comparison, actually highlight the economically harmful strategies of big box retailers. In the case of Weber, identical products sold in big boxes and local stores are labeled differently. In the case of Levi’s, a far more insidious outcome is clear; American workers were displaced as the company sought ever cheaper labor overseas in direct response to pressures from Wal-Mart.

TASK 5: SURVEY NATIONAL BRAND RETAILERS, REGIONAL PROVIDERS, AND SMALL, LOCALLY OWNED BUSINESSES TO DETERMINE THE RANGE AND SCOPE OF BOTH LABOR COMPENSATION AND LOCAL PROCUREMENT.

Social Costs

Big Box Retail in Austin does an excellent job of highlighting the low wages and attendant social costs associated with many discount big box retailers. Several studies have documented the social costs associated with Wal-Mart, perhaps the most brutal of the low-wage big boxes. The Democratic Staff of the Committee on Education and the Workforce estimates that one 200-person Wal-Mart store may result in a cost to federal taxpayers of $420,750 per year[11]. Wage compensation below what is adequate to allow employees to be self-sufficient generates cost for state and local governments as well.

However, after documenting the potential costs of these "low road" competitive strategies, the authors exile concerns over these social costs to the national level or "worthy of national dialog, [that] should play out on the national stage."

There are two problems with dismissing the social costs of low-wage big boxes as a national or federal concern. First, while many government expenditures that compensate for below self-sufficiency wages are borne by federal or state governments, certain costs do fall on local jurisdictions. Public programs to provide indigent health care, aid to low-income children, and affordable housing are examples of local programs in which low wages drive up local costs.

[11] *Everyday Low Wages: The Hidden Price We All Pay For Wal-Mart,* A Report by the Democratic Staffof the Committee on Education and the Workforce, Washington D.C: U.S. House of Representatives, February 16, 2004, page 9.

Living Wage Measures for Metro Austin

Family Security Index, Austin MSA

	1 Adult 0 Children	2 Adults 0 Children	1 Adult 1 Child	2 Adults 2 Children
Housing	$ 533	$ 645	$ 858	$ 858
Food	$ 147	$ 270	$ 206	$ 418
Childcare			$ 366	$ 569
Medical	$ 281	$ 548	$ 460	$ 727
Transport	$ 278	$ 391	$ 278	$ 391
Other	$ 177	$ 276	$ 294	$ 321
Monthly Expenses	$ 1,416	$ 2,130	$ 2,462	$ 3,284

Taxes and Tax Credits

Payroll	$ 108	$ 163	$ 188	$ 251
Income	$ 138	$ 182	$ 250	$ 298
Child Care Credit			-$40	-$83
Dependent Credit			-$40	-$80
Tax Payments and Credits	$ 246	$ 345	$ 356	$ 386

Necessary Monthly Income

Income	$ 1,662	$ 2,475	$ 2,818	$ 3,670
Household Average Wage	$ 10	$ 15	$ 17	$ 22

Necessary Annual Income

Income	$ 19,953	$ 29,694	$ 33,819	$ 44,044
Poverty Threshhold	$ 8,959	$ 11,531	$ 11,869	$ 17,463

Source: Family Security Index, Center for Public Policy Priorities, 2003

The table above provides an estimate, for various family types, of how much a full-time worker in Austin must make to pay for essential costs of living. With Wal-Mart and other low-road big box retailers paying between $8-$10 dollars per hour, often without benefits, the vast majority of their workers are not self-sufficient. This trend generates costs for housing, food assistance, childcare, and health care, a fraction of which is borne by local government. Once this "small fraction" is multiplied by the total number of non-managerial retail workers, the local costs may be significant.

Second, it is important for local governments and citizens to recognize, and perhaps give different treatment to, big box retailers who *do* provide family-supporting wages and benefits. While many national big boxes follow the low-road competitive strategy, a few compete on the "high road" of higher wages offset by higher productivity, higher quality and better service. The following table compares Costco to Sam’s, a warehouse-style chain operated by Wal-Mart. Costco manages to pay livable wages, while outperforming Wal-Mart, by treating workers better and reaping higher productivity and lower worker turnover as a result. Note that the wages listed in the chart below are for Sam’s, Wal-Mart’s warehouse-style chain; workers at Wal-Mart's conventional stores can earn substantially less per hour.

Compensation Comparisons, Costco and Sam's, 2003	Costco	Sam's
Average Hourly Wage	$ 15.97	$ 11.42
Annual Health Cost (per worker)	$ 5,735	$ 3,500
Covered by Health Plan	82%	47%
Annual Retirement Cost (per worker)	$ 1,330	$ 747
Covered by Retirement Plan	91%	64%
Employee Turnover (per year)	6%	21%
Labor and Overhead Costs (as % of sales)	10%	17%
Sales per Square Foot	$ 795	$ 516
Profits per Employee	$ 13,647	$ 11,039
Yearly Operating Income Growth (5 years)	10%	10%

Source: Holmes Stanley and Wendy Zellner, "Higher wages mean higher profits, but try telling that to Wall Street," Business Week, April 12, 2004, p.76

We argue that it incumbent upon the city to consider the social costs of low-wage national big box retailers, and to differentiate between high-road and low-road firms when considering sites, zoning variances, and general support for big box development. External costs of low worker compensation should not be borne by host communities who end up subsidizing labor for large, highly profitable corporations. These issues *cannot* be addressed through design standards.

TASK 6: ASSESS CRIME AND TRAFFIC COUNTS TO DETERMINE RELATIVE IMPACTS ON PUBLIC SAFETY AND THE ENVIRONMENT.

Among the most disappointing outcomes of *Big Box Retail and Austin* is the absence of any concrete measures of the infrastructure and public safety costs for big boxes. A number of studies and impact analyses have shown that large big box developments generate increased costs for host localities and neighborhoods. Traffic and congestion costs, street and road maintenance costs, environmental costs (runoff, storm water), public safety costs (greater than average use of police and EMS) and depressed property values in nearby neighborhoods are among the documented costs associated with big box development.

It is beyond the scope of this analysis to estimate the range of costs for increased big box development in Austin. However, the Town of Barnstable, Massachusetts, contracted for a systematic study of the net fiscal impacts of various residential and non-residential land uses in 2002. The table below provides an estimate of local operating and capital expenditures per 1,000 square feet of big box (defined as over 40,000 SF). In this analysis, the fiscal impacts of big boxes actually showed a *net loss* for the city, due to high public service and capital expenditure costs that were not offset tax contributions of big boxes.

Operating and Capital Expenditures for Nonresidential Land Uses
Town of Barnstable, Massachusetts, 2002

Annual Expenditures per 1000 Square Feet	Specialty Retail	Big Box Retail
Town and Council Manager	$ 4	$ 4
Administrative Services	$ 52	$ 56
Community Services	$ -	$ -
Police	$ 486	$ 629
Public Works	$ 200	$ 265
Regulatory Services	$ 15	$ 16
Schools	$ (81)	$ (87)
Other Operating Requirements	$ 54	$ 65
Captial Improvement Requirements	$ 55	$ 74
Total Expenditures	$ 786	$ 1,023
Total Net Revenue	$ 1,112	$ 544
Net Fiscal Impact per 1000 Sq. Ft.	**$ 326**	**$ (468)**

Source: Tischler and Associates, Inc, Fiscal Impact Analysis of Residential and Non-Residential Land Use Prototypes, Prepared for the Town of Barnstable, Massachusetts, July 1,2002

Clearly, the parameters and cost estimates would likely be different for Austin. It seems crucial, however, to obtain solid estimates of the capital expenditures and public service costs for big box development so the city can consider appropriate impact fees or negotiate compensation based on the full costs of these developments. At the very least, new retail development should not put the city in the red.

TASK 7: INTEGRATE THE ABOVE FINDINGS WITH AVAILABLE INFORMATION ON "BEST PRACTICES" REGARDING PUBLIC POLICY ON LAND USE RELATED TO RETAIL TO MAKE POLICY RECOMMENDATIONS.

Communities across the U.S. have recognized that unregulated big box development generates external costs and have taken actions to limit these costs. Our very limited review of the case record revealed at least 19 cities, towns or counties that had imposed regulations and/or specific mitigation fees on big box developments that went beyond design standards to address economic impacts.

In sum, the literature and record of community studies strongly suggest that big box retail development incurs significant costs that must be weighed against anticipated benefits (cheaper prices and presumed increased sales and property tax revenues) to local communities and governments. These include:

- *High Infrastructure Costs:* Big box development generates increased traffic and congestion costs, street and road maintenance costs (especially due to increased truck traffic on access roads), water and sewer costs, street and access improvement costs.

- *High Public Safety Costs:* Several studies have suggested that big box retailers generate higher local public safety costs than conventional retail. Layout, location, extended hours of operation and zero-tolerance policies toward shoplifting may generate a higher rate of police calls for big boxes. Scale, access, and parking lot design may also generate more responses to minor traffic accidents by local police and EMS. These higher service costs must also be considered against the tax revenue contributions touted by big box developers.

- *Environmental Costs:* Big box development generates high site-related environmental costs especially for storm-water drainage and construction-related groundwater pollution. In addition, high traffic generation contributes to air and noise pollution, and paved parking lots, typically topping 20 acres, contribute significantly to the “heat island” effect.

- *Neighborhood Costs:* Big box development generates traffic congestion and noise and light pollution that can adversely impact nearby neighborhoods. Poorly designed big boxes may also undermine the fabric of a neighborhood by creating unsightly, poorly integrated eyesores. These factors may combine to reduce property values (relative to values that would exist without big box development) in nearby blocks or neighborhoods. These negative net impacts on proximate property values should also be considered against the tax revenues directly generated by a development.

- *Effects on Local Retail Markets:* Big box development, if not intelligently managed, can crowd out locally owned retail. The preponderance of evidence shows that the rapid expansion of national big box retailers *has* cut into locally-owned retail in a number of markets. The loss of local retail sales and employment must be considered against gains in sales, employment and tax revenues associated with big box expansion. Because local merchants tend to purchase more from local suppliers, local retail losses have a greater impact on the local economy than national big box sales.

- *Social Costs Borne Locally:* As noted in *Big Box Retail in Austin* and in the above discussion, many big box retailers rely on low levels of employee compensation to sustain their competitive advantage. Workers who do not receive wages and benefits adequate to make them self-sufficient must rely on other work, additional family income, or taxpayer-funded benefits to make end meet. This business model generates substantial social costs, some of which are borne by local governments and institutions.

Mitigating Costs

Under current law and policy, the City of Austin has three main mechanisms to mitigate the specific costs and effects of big box development:

1. Impact fees or negotiated exactions
2. Design standards that may be incorporated into ordinances or zoning regulations
3. General and specific zoning regulations on commercial property or land uses

In their current or proposed form, these mechanisms are not, in our view, up to the task of fully mitigating the external costs of big box development. We will first discuss the limitations of impact fees and possible design standards and then briefly outline some policy recommendations that might allow the city to better manage and mitigate the costs of big box development in the future.

Impact Fees

To the extent that a local government can document the marginal costs created by a development, a local unit may be able to impose impact and linkage fees. However, we would have to consider the specific statutory requirements on “impact fees,” defined in Chapter 395 Texas Local Government Code (including roadway, water, storm water, drainage, and flood control facilities). We must also consider constitutional law constraints that may make it difficult to charge mitigation fees for diffuse social costs.

In determining exactions based on individual circumstances, the City is required to measure that impact in a meaningful, though not precisely mathematical way, and must show how the impact, thus measured, is roughly proportional in nature and extent to the required improvements. (For a recent discussion of the constitutional constraints see Town of Flower Mound, Texas v. Stafford Estates Limited Partnership, 47 Tex.Sup. J. 497 (2004)).

Design Standards

Design standards currently under development by city staff may help mitigate certain site and non-site specific costs of big box development. Depending on what form they take, design standards might be effective at controlling negative neighborhood effects, as well as problems with traffic and accessibility outside the purview of impact fees.

However, several key cost elements of big box development cannot be addressed through design standards. Negative effects on local retail markets, social costs borne locally and higher public safety costs would seem to be outside the purview of new design standards for big boxes.

Zoning

Because impact fees and proposed design standards cannot alone address the serious economic impacts of increased big box development, perhaps the strongest tool available to Texas cities is zoning. State law grants cities broad authority to zone for purposes of “ … promoting the public health, safety, morals or general welfare…” of communities. Cities have specific authority to regulate many issues relevant to sound city planning including building height, size, location, and use, as well as density and open spaces (Chapter 211, Texas Local Government Code).

Austin’s Land Development Code, like that of most cities, was drafted well before anyone envisioned stores exceeding 50,000 square feet, let alone the 200,000 square-foot supercenters of today. Given dramatic increases in store size over the past 15 years and the well-documented costs of these enormous structures, it seems reasonable to require a Conditional Use Permit for all new, large-scale chain retail developments. If adopted, such a measure would give the city a strong planning tool to shape and guide placement of mega-stores, preventing sales leakage at the city borders while limiting the overall negative effects to our economy and residents.

Recommendations for Further Policy Consideration

Below we outline recommendations intended to help the city manage and offset costs and to provide for sensible placement and planning of big boxes in our community. We advance these policy initiatives for broad consideration only, understanding that detailed elements would need to be fleshed out by city staff and legal counsel.

1. **Require a Conditional Use Permit for all proposed large-scale retail developments, including an impact analysis to demonstrate net benefits and costs to the community, with the possibility of negotiated exactions to mitigate substantial costs.** Based on the recently adopted Los Angeles model, such an analysis may include:

    - Estimated cost to the City for additional public safety, infrastructure, and traffic;
    - Anticipated effects on existing businesses;
    - Estimated net gains/losses for property tax and sales tax revenues
    - An employment plan for the first year of operation, including job titles, the number of employees anticipated in each job title, and wage and benefit packages;
    - Anticipated costs for public health care and housing for workers if salaries do not meet the Family Security Index (FSI) as calculated for the Austin area (see page 17);
    - Architectural renderings showing all four sides of the structure, signage, and landscaping in conformance with whatever design standards the City may subsequently adopt;
    - A plan for the re-lease, reuse, or sale of vacated structures to prevent abandoned big boxes from undermining commercial areas.

2. **Develop long-term strategies to strengthen and enhance our local retail market.**

    - Regarding major employers, the City should amend its economic incentives policy so that incentives are available only to companies paying wages and benefits that allow employees to be self-sufficient.
    - Develop policies that provide strong support for local independent businesses. For example the Austin Independent Business Alliance proposal for Independent Business Investment Zones is worth considering.
    - Identify the current market share of all big box retailers in Austin, not limited to the six specific retailers in the current study, with the goal of establishing a diverse retail balance to sustain a healthy, competitive market. As a starting point, use the Columbia University definition of “big box.”

- Explore a regional compact as a means to ameliorate tax incentive competition among area jurisdictions to capture retail activity, thereby reducing “beggar thy neighbor” impacts.

In conclusion, we would posit that the above analysis and recommendations do not constitute unreasonable demands or burdensome regulations on big box retailers. Indeed, a basic principle of market economics is that *business firms should carry the full costs of producing or selling their products.* Violation of this principle damages the operation of competitive markets; if some external costs are borne by third parties, as outlined in both the original study and this analysis, this creates an implicit subsidy that unfairly lowers the prices of the subject firm below true marginal costs. Requiring companies to carry the true costs of their own business is perfectly consistent with the fair and efficient operation of the free market.

POINT-BY-POINT REVIEW OF CITY STUDY MAJOR FINDINGS

Big Box Retail and Austin, prepared by TXP, Inc., presented eleven findings and a general conclusion to the Austin City Council on June 24, 2004. This document compares each finding with the response by Dan Houston, Michael Oden, and Bill Spelman.

Note that this comparison does not correspond to the seven key tasks originally assigned by Council, but to the Summary of Findings and Conclusions presented on pages 3-7 of *Big Box Retail and Austin.* Specifically, it does not address an assigned key task omitted from the final report, the assessment of crime data and traffic counts related to big box development. For information on this issue, please see pages 18-19 of the Independent Review above.

City Finding #1: "Big boxes create consumer value through lower prices."

In supporting this finding, the authors state: "The benefit to consumers is straightforward - as reported by Bianco and Zellner in *Business Week*, "New England Consulting Group estimates that Wal-Mart saved its U.S. customers $20 billion last year alone. Factor in the price cuts other retailers must make to compete, and the total annual savings approach $100 billion."

> **PARTIALLY DISAGREE: Big boxes often offer low prices, but the total net benefits to consumers are hardly straightforward; further, the figures cited in the study are not verifiable.**
>
> Big box prices are indeed low and have driven down prices across many retail segments. Lower prices undoubtedly benefit consumers by stretching their retail dollars. However to some extent, low prices and associated consumer benefits are made possible by low wages, poor working conditions, and large, cheaply built facilities that generate costs to individuals and communities. While prices may appear low, many chains pass on substantial invisible costs to taxpayers and communities. These include: subsidized housing, health care and other services for low-wage workers; increased public safety and infrastructure costs; and jobs lost to offshore suppliers. In essence, host communities end up subsidizing large, highly profitable corporations.
>
> Regarding the $20 billion estimate of national consumer savings, the authors acknowledged in the June 24, 2004, City Council presentation that they "cannot verify that number" and that New England Consulting Group was "unwilling" to share information about how it arrived at this figure.

City Finding #2: "There appears to be relatively little direct competition between big boxes and local retailers; where competition exists, prices

tend to be comparable. In general, locally owned retailers employ a different business model to succeed."

> **STRONGLY DISAGREE: Evidence presented by study authors is insufficient to support the claim of "little direct competition."**
>
> The preponderance of evidence in academic literature and specific impact studies suggests that a rapid increase in big box retail *does* negatively affect many types of smaller scale local retail. The fact that local retail survivors have been pushed into a new niche or significantly changed their business tactics does not equate with "little direct competition." This claim also fails the basic reality test, as a ten-minute conversation with any local retailer will likely reveal.

City Finding #3: "All big boxes are not identical, and shifts in consumer preferences may widen these differences going forward."

> **AGREE: Certain big box chains do demonstrate significantly greater corporate responsibility in terms of wages and costs to taxpayers; consumers *and* communities should demonstrate an active preference for these companies, where possible.**
>
> Costco is an excellent example of a big box chain that offers employees a livable wage and benefits package, greatly reducing the costs to taxpayers and host communities. Clearly, it makes sense for communities - as well as consumers - to give preference, where possible, to big boxes that pull their own weight financially, while discouraging those that generate greater costs to the community.

City Finding #4: "The healthiest consumer market is the market that maximizes consumer choice on a sustainable basis, i.e., a market that is competitive."

Here the authors cite the Herfindahl-Hirschman Index to determine market concentration and then state that big boxes represent only 21.2 percent of the current Austin market, noting this figure "is still well below a level that suggests competition is being undermined."

> **DISAGREE WITH DATA AND FINDING: The 21.2 percent market share cited by the authors is a misleadingly low figure, shaped by the authors' unorthodox definition of big box, which limits their inquiry to six specific retailers.**
>
> A more accepted definition, such as the one formulated by Columbia University and initially cited by the authors, would include many other widely recognized big boxes such as Circuit City, Office Max and Best

Buy. Using this more common definition would reveal that big boxes already control a much larger market percentage in Austin. For example, based on figures provided in the study, Home Depot and Lowe's combine for roughly 50 percent of the local market in building materials - clearly a more alarming figure if diverse retailing and sustainable competition are the goals.

Regarding competition, we also note a basic principle of market economics that *business firms should carry the full costs of producing or selling their products.* If external costs for some firms are borne by third parties, as detailed in Response #1 above, this creates an implicit subsidy, skewing the playing field for others and ultimately weakening fair competition.

City Findings 5 & 6: "New Urbanist land use policy...offers the possibility of mitigating some of the concerns associated with the big boxes, as well as potentially creating an opportunity to leverage destination consumers for local businesses … The City should promote design standards that reflect community values."

DISAGREE REGARDING ECONOMIC IMPACTS. While we support stronger design standards for large retailers, more stringent design standards will not cure many of the negative economic impacts of unfettered big box development.

To address economic issues, we must be willing to explore market-based strategies that will encourage businesses that offer overall economic benefits to Austin, while limiting or discouraging those that bring a high cost to our community.

City Finding #7: "Big boxes put downward pressure on wages."

AGREE. As the cost of living in Austin continues to rise, our city can ill afford the additional downward pressure on residents' wages associated with the majority of big box chains.

We must explore policies that give our citizens the best advantage in today's job market.

City Finding #8: "Lower wages tend to create social costs that are not fully accounted for in the price of the goods that consumers purchase."

AGREE. These well-documented social costs - including health care, housing, food, and child care - are ultimately borne by taxpayers and host communities.

A recent Congressional report found that each 200-person Wal-Mart store costs taxpayers over $420,000 per year in subsidies for underpaid workers.[12] As a community, we should be rightly reluctant to subsidize fair labor costs for large, highly profitable corporations.

City Finding #9: "Local retailers may have stronger linkages, per dollar of revenue, to the local economy than big boxes."

AGREE: It is well-documented that local retailers offer much stronger support for local economies than do national chains; city policies should be crafted to strengthen and enhance local retailers.

This fact has been documented in several studies, including one conducted locally, which found that $45 of every $100 spent at a locally-owned store stays in the community vs. only $14 for every $100 spent at a national retailer. Policies that support local retailers will in turn strengthen our local economy.

City Finding #10: "Small local retailers enhance the local economy over and above the value created for consumers through contribution to the area's cultural vitality."

AGREE. The continued success of Austin as a retail hub for the region will be based on sustaining and burnishing our unique retail base.

While big boxes will undoubtedly remain part of our retail mix, a sophisticated strategy would involve more support for unique local retail establishments and districts, while guiding, and in select cases limiting, unfettered development of big boxes in Austin.

City Finding #11: "The local fiscal impact of retail is a function of maintaining a retail base that can meet local demand."

This finding notes that consumers tend to shop close to home, but states that near the city limits "leakage" may occur, in which consumers cross municipal boundaries to shop.

DISAGREE WITH DATA AND FINDING. Inaccurate numbers released in the original report paint a false picture of suburban retail drain; in fact, Austin significantly outperforms suburban jurisdictions for retail sales.

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[12] *Everyday Low Wages: The Hidden Price We All Pay For Wal-Mart,* A Report by the Democratic Staff of the Committee on Education and the Workforce, Washington D.C: U.S. House of Representatives, February 16, 2004, page 9.

In their original calculations, the authors estimated that Austin's share of regional retail activity had fallen from 83.5% to 53.9% in the last 13 years, seeming to indicate a precipitous trend. However, when these figures are corrected for actual retail sales (rather than "sales tax allocations," which disregards differing sales tax rates in each jurisdiction), it is clear that Austin is significantly outperforming suburban jurisdictions. In 1990, Austin's share of the metropolitan population stood at 56%, yet city stores accounted for 88% of regional retail sales. By 2003, city population was at approximately 50% while city stores still accounted for 69% of all retail sales in the metropolitan area - a healthy ratio by anyone's standards. Rather than creating a sense of desperation to remain competitive, these corrected figures should lead to a discussion of why urban retail is so vibrant in Austin and how those advantages might be further supported and developed.

More strategic policies for the development of big box retail in Austin would keep negative economic impacts to a minimum while holding sales tax revenues within the city limits.

CITY STUDY CONCLUSION: The authors dismiss the city's role in addressing economic and social concerns, relegating these issues to "play out on a national stage." They then outline three broad goals for the city:

(a) Insure continued capture of "fair share" of total local retail demand and insure market share of local retailers remains "at least consistent;"
(b) Recognize contribution to cultural vitality by local retailers through proactive assistance; and
(c) Work with development sector and other stakeholders to ensure that community goals and business needs are integrated into any ultimate regulatory scheme for retail design and urbanism.

INDEPENDENT RESPONSE: The authors' dismissal of economic and social concerns to the national level troubles us for two reasons. First, the majority of big box retailers do generate specific costs for local jurisdictions, including greater service costs for police and EMS, indigent health care, affordable housing and increased public safety and infrastructure costs. Second, it is important for local governments and citizens to recognize, and where possible give preference to, big box retailers who do provide family-supporting wages and benefits.

Regarding the study's recommended goals:

(a) As previously noted, we believe the study's figures are incorrect for both Austin's share of regional retail activity and the current market share for big boxes in Austin. Corrected figures point to different policy conclusions, including limiting and shaping future big box development.

(b) We fully concur with the recommendation that the city develop and offer increased proactive support for local retailers.
(c) We strongly question the conclusion that the principal concern of city government should be in establishing design standards for a subset of big box establishments. Market-based strategies are needed to address the well-documented negative economic impacts associated with unfettered big box development.

ABOUT THE AUTHORS AND SPONSORS

Big Box Retail and Austin: An Independent Review has been a team effort among the three authors and the three sponsoring organizations.

About the Authors

Dan Houston is a partner in the firm of Civic Economics, an economic analysis and strategic planning consultancy with offices in Austin and Chicago. In the two years since its founding, the firm has established a nationwide reputation for creative approaches to economic development challenges, bringing its unique approach to sustainable prosperity to eleven states in the United States and Mexico. The firm has also developed specialized expertise in studying the dynamics of localized retail and service provision. Before establishing Civic Economics, Mr. Houston served as Senior Project Manager for economic development at Angelou Economics in Austin.

www.CivicEconomics.com

Dr. Michael Oden is an Associate Professor of Community and Regional Planning in the School of Architecture at the University of Texas at Austin. Dr. Oden's teaching and research areas include local and regional economic development, regional growth dynamics, program evaluation methodologies, and affordable housing policy. Prior to joining Community and Regional Planning (CRP) program he worked at the Project on Regional and Industrial Economics at Rutgers University, the Organization of Economic Cooperation and Development in Paris, and as the senior economist on the Appropriations Committee of the Michigan State Senate.

wnt.utexas.edu/architecture/people/faculty/odenf.html

Dr. William Spelman is a Professor of Public Affairs in the Lyndon Baines Johnson School of Public Affairs at the University or Texas at Austin. An urban policy specialist, Dr. Spelman holds a Ph.D. in public policy from Harvard University's John F. Kennedy School of Government. He has a background in operations research and evaluation and in local government law, administration, and finance. Dr. Spelman served on the Austin City Council from 1997-2000, and has served the community in a variety of volunteer positions, including the Board of Directors for Liveable City.

www.utexas.edu/lbj/faculty/spelman.html

About the Sponsoring Organizations

The **Austin Independent Business Alliance** is a voluntary association representing the interests of over 300 locally owned businesses in the Austin area.

www.Austin-IBA.org

Austin Full Circle is an all-volunteer coalition of business, labor, environmental, and neighborhood leaders focused on corporate responsibility and the economic impacts of increased big box development.

www.AustinFullCircle.org

Liveable City is an inclusive network of individuals working together to create a community consensus to promote policies that address the long term social, environmental, and economic needs of the people of Austin.

www.LiveableCity.org

American Federation of State, County, and Municipal Employees Local 1624 is a local union representing employees of the City of Austin and Travis County and an advocate for sustainable wages and benefits for working people throughout the community.

www.AFSCME1624.org

The ANDERSONVILLE STUDY of Retail Economics

October 2004 Chicago, Illinois

Modified February 2005

CIVIC ECONOMICS

CREATIVITY · OPPORTUNITY · PROSPERITY

HIGHLIGHTS OF THE ANDERSONVILLE STUDY

In a study comparing the economic impact of ten Andersonville businesses and their chain competitors, it was found that:

Locally-owned businesses generate a substantial Local Premium in enhanced economic impact.

- For every $100 in consumer spending with a local firm, $68 remains in the Chicago economy.
- For every $100 in consumer spending with a chain firm, $43 remains in the Chicago economy.
- For every square foot occupied by a local firm, local economic impact is $179.
- For every square foot occupied by a chain firm, local economic impact is $105.

Consumers surveyed on the streets of Andersonville strongly prefer the neighborhood over agglomerations of common chain stores.

- Over 70% prefer to patronize locally-owned businesses.
- Over 80% prefer traditional urban business districts.
- Over 10% of respondents reside outside the City of Chicago.

The study points to clear policy implications.

- Local merchants generate substantially greater economic impact than chain firms.
- Replacement of local businesses with chains will reduce the overall vigor of the local economy.
- Changes in consumer spending habits can generate substantial local economic impact.
- Great care must be taken to ensure that public policy decisions do not inadvertently disadvantage locally owned businesses. Indeed, it may be in the best interests of communities to institute policies that directly protect them.

www.AndersonvilleStudy.com

EXECUTIVE SUMMARY

Abstract:

The Andersonville Development Corporation, with the support of The Andersonville Chamber of Commerce and funding by Andersonville Special Service Area #22, retained Civic Economics to evaluate the economic impact of the neighborhood's locally-owned businesses and compare that with the impact of competitive chains. With the active participation of ten local firms, economic impacts were determined for each. Economic impacts for ten chains were then determined. To account for differences in revenue and size, those impacts were adjusted to two measures: impact per $100 revenue and impact per square foot. Because the locally-owned businesses and national chains were found to generate comparable revenue per square foot of retail space, the local firms were found to generate 70 percent greater local economic impact than chains per square foot, or 58 percent by revenue.

ANDERSONVILLE

Photo © Andersonville Chamber of Commerce

Andersonville is a neighborhood on Chicago's north side. Its primary thoroughfare, Clark Street, bisects the neighborhood and serves as its commercial center. The commercial district is distinctive for its quaint facades and greenery, its history as a Swedish settlement, its current diversity, and the notable dearth of chain outlets among its countless shops, restaurants, and service providers. However, national chains have expressed interest in the community as disposable income continues to increase. These national chains are able to pay above present market value on their leases, which has begun driving commercial rental rates up and longstanding local businesses out.

The Andersonville Development Corporation (ADC), the Andersonville Chamber of Commerce (ACC) and Andersonville Special Service Area provide economic and market development services to the area. Civic Economics is an economic analysis and strategic planning consultancy with offices in Austin and, coincidentally, Andersonville.

Civic Economics previously conducted a widely cited study in Austin, Texas, assessing the economic impact of a publicly subsidized Borders Books & Music store seeking to locate across the street from locally-owned Book People and Waterloo Records. In those unique circumstances, it was demonstrated that the local merchants generated three times as much local economic activity as the chain store, adjusted for revenue. That study, known as the Liveable City Study, has been replicated in two very different circumstances with similar findings: Maine's Mid-Coast region and Toledo, Ohio.

ADC retained Civic Economics to build upon that research, studying the role of Andersonville's diverse business community in the Chicago economy. ADC recruited ten local businesses to participate fully in the study, opening their books to the firm to facilitate a complete economic impact analysis of each. Civic Economics then prepared economic impact analyses of ten chain competitors selected in consultation with ADC and with consideration given to data availability. We adjusted those impacts to account for variations in revenue and square footage, and, to further explore the meaning of the data, businesses were categorized into three segments: restaurants, retailers, and service providers.

ADC also conducted a Customer Preference Survey of 512 randomly selected shoppers within the neighborhood during the month of May 2004. While this was an unscientific survey it provided interesting background information about where patrons are drawn from and why they choose to shop in Andersonville. Just under 40 percent of survey respondents came from outside the two main zip codes for the Andersonville area, and ten percent were from outside the City of Chicago. These visitors bring money into the district and into the city.

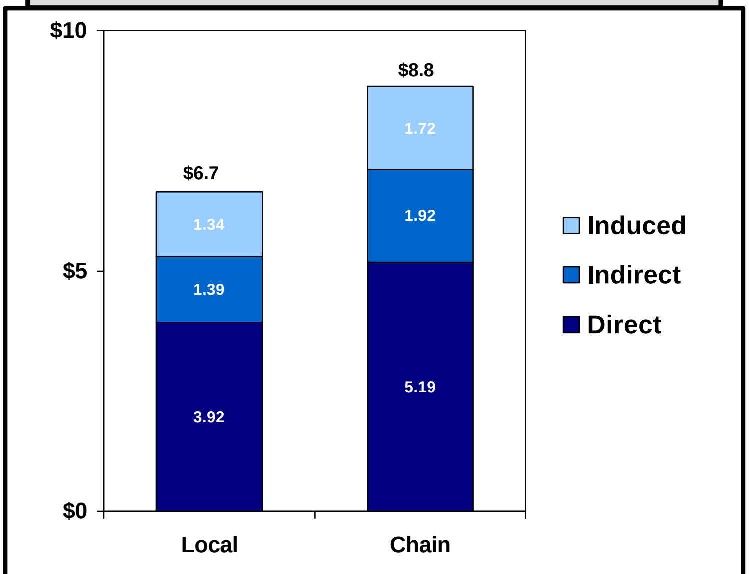
When asked to express a preference on the type of business shoppers patronize, over 70 percent preferred locally-owned businesses while less than three percent preferred chain businesses. Additionally, an overwhelming 80 percent of respondents identified Andersonville's traditional neighborhood district, with locally-owned independent businesses, as their preferred shopping environment.

These results lend support to the preexisting belief in the neighborhood that the unique businesses and layout of Andersonville are a draw, attracting people from both inside and outside the region. Visitors are consciously choosing this type of commercial district over others.

Aggregate Economic Impacts

Using the City of Chicago as the relevant jurisdiction, economic impacts were calculated and aggregated (all local businesses and all chain businesses). Including direct, indirect, and induced effects, we found that the ten local firms generate a combined $6.7 million in annual economic impact compared to $8.8 million for the ten chains.

LOCAL IMPACT COMPONENTS (millions)



SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

In this case, *direct* effects reflect the first round of local spending, such as wages and benefits, profits to local owners, local procurement, and charitable contributions. *Indirect* and *induced* effects reflect the continuing circulation of that first round of spending by businesses and individuals respectively.

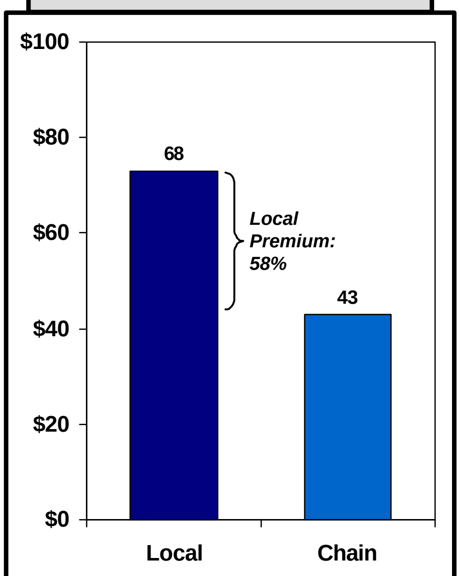
Local economic impacts for businesses that serve a local market are primarily made up of four components: labor, profit, procurement, and charity.

Looking only at the chart above, the simplest policy conclusion jumps to the fore: these ten chain businesses create greater economic impact than the ten local firms. However, the following pages demonstrate that this simple assumption neglects to account for two essential variables: the revenue and square footage of each business. These variables, as we shall see, thoroughly erase the apparent economic impact advantage of chain businesses.

Adjusted Economic Impacts

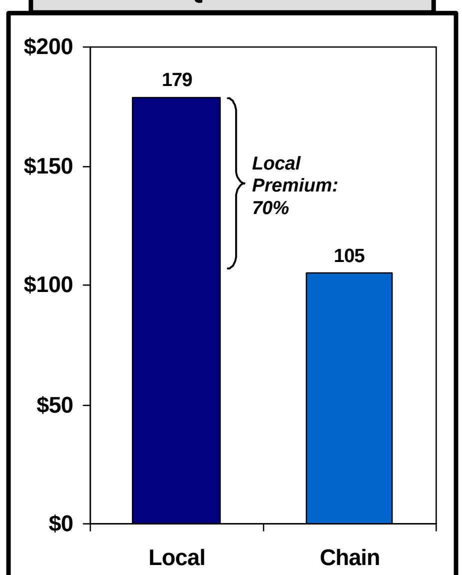
Among the firms studied, chain businesses took in an average of over twice the revenue and occupied twice the square footage of the locals. Therefore, it was necessary to adjust raw economic impact values to account for these substantial differences. When those adjustments are made, the apparent economic impact benefit of the chain businesses is completely erased. The fact that locally-owned businesses ($263 revenue per square foot) and national chains ($243 revenue per square foot) generated comparable sales per square foot of retail space negates any size advantage the chains have over their locally-owned competitors.

LOCAL IMPACT
PER $100 REVENUE



SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

LOCAL IMPACT
PER SQUARE FOOT



SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

For every $100 in consumer spending with chain firms, $43 will remain in the local economy; if that same spending occurs with a locally-owned firm, that value jumps by 58 percent, to $68. Similarly, for every square foot of space occupied by a chain, the local economic impact is $105; if a local firm occupies that same space, impact jumps by 70 percent, to $179.

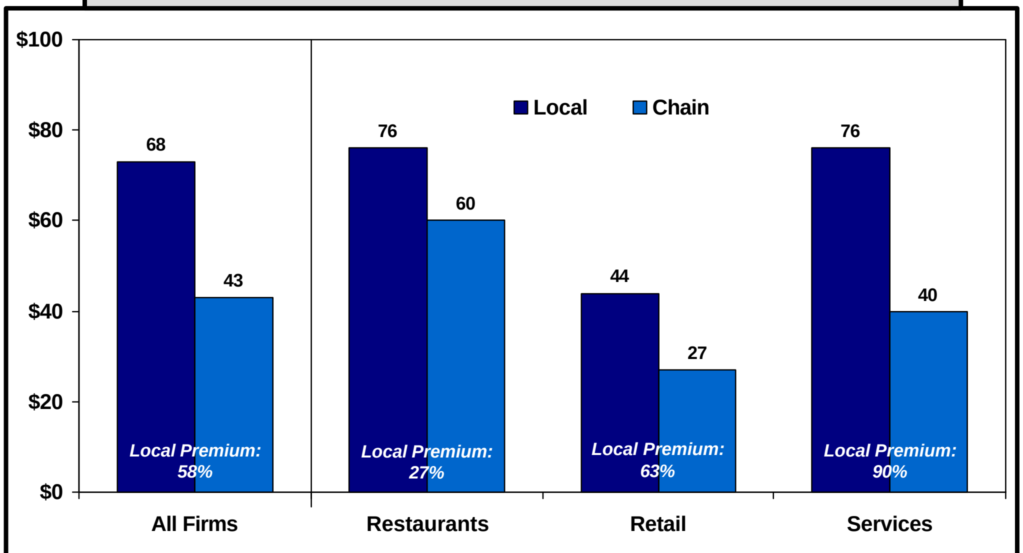
This Local Premium represents the quantifiable advantage to the city provided by locally-owned businesses. Whether measured as a share of revenue or by square footage, local firms generate a substantial Local Premium over their chain competitors. That means more money circulating in the local economy, which may mean more home improvement, more in the collection plate, and more in taxable transactions to fund city services.

Across the board, locally-owned businesses substantially exceed their chain competitors in all four components. For example, local firms spent an average of 28 percent of revenue on labor compared to 23 percent for chains. Additionally, eight of the ten local firms are owned by Chicago residents, so profits largely remain in the city. Local firms procure local goods and services at more than twice the rate of chains. Finally, locally-owned firms in the study contribute more to local charities and fundraisers than do their national counterparts and, although this provides the smallest local advantage of the four categories, this difference is important to the community.

Economic Impacts by Sector

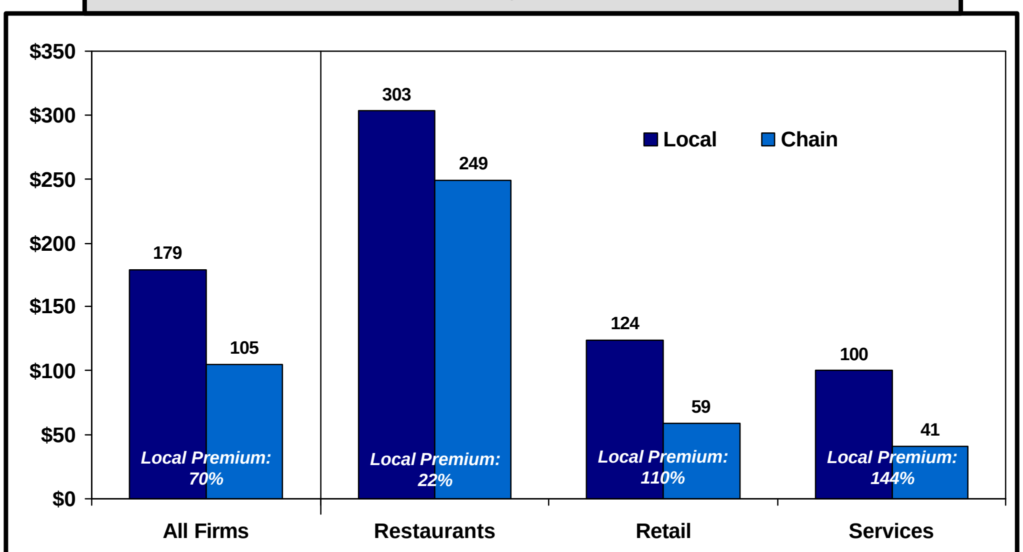
In order to gain a fuller understanding of these results, businesses were further categorized as restaurants, retailers, and service providers. This further analysis reveals that the Local Premium ranges from 144 percent per square foot among service providers to 63 percent among retailers and 22 percent per square foot among restaurants.

LOCAL IMPACT PER $100 REVENUE BY SECTOR



SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

LOCAL IMPACT PER SQUARE FOOT BY SECTOR



SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

These differences are largely accounted for by one factor: labor costs. Restaurants, for example, are heavily dependent on employed labor. Locally-owned restaurants tend to employ more workers, have them work slightly longer hours, and pay them slightly more than their chain competitors. Local service providers, at the other end, are heavily dependent on the labors of the owner while their chain competitors rely more on employees, resulting in the most substantial Local Premium.

Policy Implications

A careful reading of the data demonstrates that locally-owned businesses provide substantial economic benefits to the city, benefits that are in danger of being measurably diluted by increasing chain competition. While fair competition and consumer choice are the touchstones of urban economics, great care must be taken to ensure that public policy decisions do not inadvertently disadvantage local firms. Indeed, it may well be in the best interests of communities to institute policies that protect them.

Andersonville is a model for prosperous communities nationwide. There, Chicagoans offer a wide array of products and services, keep local dollars in the local economy, and contribute to Chicago's privileged place among American cities. But Andersonville and the dozens of neighborhoods like it are particularly threatened by the proliferation of chain businesses.

Future public policies in Chicago must seek to protect and promote the Andersonville model rather than facilitate its demise. Equally important is the matter of consumer choice. With each purchase, consumers put into play their hard earned dollars; the consumer's decision to patronize a local firm versus a chain competitor ripples through the economy with dramatic results.

COMPLETE REPORT

The complete analysis is presented in four sections as follows:

- **INTRODUCTION AND BACKGROUND** – putting the Andersonville Study in context, describing previous related studies and the origins of this one
- **METHODOLOGY** – outlining the analytical process followed by Civic Economics
- **FINDINGS** – presenting the results of this analysis through four steps:
    - Components of Local Economic Impact
    - Aggregate Economic Impacts
    - Adjusted Economic Impacts
    - Economic Impacts by Sector
- **POLICY IMPLICATIONS** – describing some practical applications of these findings for consideration by policy makers and consumers

INTRODUCTION AND BACKGROUND

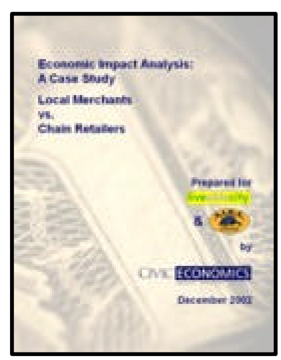
Civic Economics, the Andersonville Development Corporation, the Andersonville Chamber of Commerce, and Andersonville Special Service District Number Twenty-Two collaborated on this study, designed to evaluate the regional economic role played by independent businesses in this dynamic district on Chicago's North Side.

In short, the study was designed to calculate the economic impact of Andersonville's locally-owned businesses and assess the economic impact of increasing chain store activity in the region. Ten Andersonville businesses agreed to participate fully in the study, opening their books to analysts at Civic Economics in order to allow a thorough understanding of their revenue and expenses. In addition, the study included a survey of consumers visiting the Andersonville area.

Battles between national chains and local merchants have been raging for some time now. The argument for supporting local merchants has often been an emotional one, pleading for support in the name of intangible qualities associated with buying local: superior customer service, involvement in community affairs, wider range of quality goods, and personal attention. While these factors are important, the economic benefits that chains are able to claim, such as employment numbers and sales tax collections, may overwhelm even well intentioned and informed public officials who believe chain stores benefit the community more than do locally-owned stores.

The partners at Civic Economics contended that the emotional argument put forth by local merchants should be supplemented by solid economic research. We suspected that while the large national chains generated more revenue from sales, much of this money left the region in which it was generated. Civic Economics found a perfect test case in Austin, Texas to explore the theory.

Background - The Liveable City Study and beyond



The Andersonville Study is designed to build on a series of research that began in Austin, Texas in 2002. There Civic Economics was hired by the Austin Independent Business Alliance and nonprofit Liveable City to design and execute a limited study evaluating the likely economic impact of a big box outlet proposed for a corner already occupied by large local merchants selling identical goods.

Austin has faced a range of contentious choices in recent years. The community spirit has long been defined by the city's quirky personality, but explosive growth has dramatically changed the city. Contemporary notions of prosperity have threatened to transform Austin into another Houston or Dallas, with live music and technological prowess reduced to economic development and tourism marketing hooks.

However, these forces have met with strong local resistance. One recent battleground was the intersection of Sixth & Lamar, at the western edge of the historic urban core. There, in the shadow of beloved local merchants BookPeople and Waterloo Records, a developer proposed to erect a strip center anchored by Borders Books & Music. Moreover, the city's complex smart growth ordinance resulted in development incentives exceeding $2 Million. Opposition to the development was emotional and shrill, providing little basis on which prudent city officials might step in and change the outcome.

The Civic Economics partners saw an opportunity to inject facts into the dialogue, providing public officials with a legal basis on which to act. We formulated a methodology and presented the idea to the local merchants involved. The merchants signed on, and additional funding and public relations support for the study were provided by Liveable City and the Austin Independent Business Alliance.

While the study began with no preconceived notions, the findings were remarkable:

> *For every $100 in consumer spending at Borders, the total local economic impact is only $13. The same amount spent with BookPeople or Waterloo Records yields more than three times the local economic impact, or $45.*

Building on that analysis, Civic Economics formulated three essential findings:

- Local merchants generate substantially greater economic impact than chain retailers.
- Development of urban sites with directly competitive chain merchants will reduce the overall vigor of the local economy.
- Modest changes in consumer spending habits can generate substantial local economic impact.

Since the release of the Liveable City Study[1], the work has been replicated in two communities. The Institute for Local Self-Reliance found nearly identical results in a study of retail activity in Mid-Coast Maine[2], and the University of Toledo[3] Urban Affairs Center found comparable results in a study of bookstores in Lucas County, Ohio. However, given the narrow focus of these studies, there has been no clear and accepted consensus regarding the applicability of these findings in other settings. Indeed, Civic Economics has repeatedly cautioned against

1 Available for download at http://www.civiceconomics.com/Andersonville/Lamar_Retail_Analysis.pdf
2 Available for download at http://www.newrules.org/retail/midcoaststudy.pdf
3 Available for download at http://uac.utoledo.edu/Publications/Toledo-Merchant-Study-04.pdf

assuming the Liveable City findings were universal, given the unique attributes of the local merchants studied.

Civic Economics In Andersonville

The Andersonville neighborhood on Chicago's north side presents an ideal extension of the work begun in Austin. With its cohesive neighborhood organizations, dedicated and involved residents, and dense, thriving commercial district, Andersonville was an able and enthusiastic test subject.

Andersonville has become one of Chicago's most popular neighborhoods. From its beginnings as a Swedish enclave through today, its Clark Street core of unique, locally-owned businesses has been one of the main drivers of the community's success. However, its appeal is attracting increased interest from numerous chain stores looking to locate an outlet on Clark Street. Both residents and business owners are deeply concerned that the possible change in the neighborhood's character would be detrimental to both the quality of life and the commercial viability of the community.

The Andersonville Development Corporation and the Andersonville Chamber of Commerce were in search of empirical data to show whether a strategy of encouraging locally-owned, independent businesses was prudent and economically sound. The Development Corporation retained Civic Economics to study the impact of existing local businesses and compare that to prospective national competitors. This study was designed to provide more definitive answers required for the formulation of new urban development policies and the preservation of Andersonville's economic vitality.

METHODOLOGY

The Andersonville Study of Retail Economics was designed to measure the economic impact of twenty businesses, ten locally-owned firms operating in Andersonville and ten chain firms loosely identified as competitors or prospective competitors.

The first step in this process was to pick the actual companies from Andersonville that would comprise our local components. After consultation among the Andersonville Development Corporation, Andersonville Chamber of Commerce, and Civic Economics, it was decided that the companies should meet the following criteria:

- Located within the physical boundaries of the Development Corporation and Chamber of Commerce service areas
- Representative of the variety of retail, restaurant, and service firms that serve the neighborhood
- Drawn from throughout Andersonville's mile-long Clark Street commercial corridor
- Representative of the cultural and ethnic diversity of the community

Additionally, as there are several locally-owned franchises that serve the community, we decided that at least one locally-owned franchise should be included to ascertain where these firms fit in the local-chain dynamic.

Once these ten local firms were chosen, chain competitors were identified. The national competitors were chosen using the following guidelines:

- Offering the same general product line or service as a local firm
- Not located in Andersonville
- Publicly held, to ensure the availability of data
- Not headquartered in Chicago

The following chart shows the local and chain businesses ultimately selected for participation in the study:

ANDERSONVILLE STUDY FIRMS BY SECTOR

	Restaurant	Retail	Service
Local	Andies M Henry Star Gaze Swedish Bakery	Chicago Aquarium White Hen Women & Children	Joel Hall Toujours Visionary
Chain	Applebee's Denny's Olive Garden Panera	Petco Convenience Store Borders	Cinemark Supercuts Pearle

Three notes are appropriate regarding the chain businesses selected for study. Many of these corporations operate a mix of corporate-owned and franchised outlets; in those cases, the analysis covers only corporate outlets. For Cinemark, calculations assume a four-screen facility. Due to difficulties separating corporate and franchised convenience stores, we formulated data for a hypothetically average, corporate-owned convenience store of 2,000 square feet.

After the local and national matches were made, the interview process began to gather the data needed from the local companies. These interviews were conducted face to face with owners or representatives of the local businesses. Worksheets were designed to elicit total revenue and expenditure patterns for each firm, including supplier locations and employee residence.

These owners provided data, which we treated as confidential, addressing the four primary areas where these firms expend funds locally: labor, profit, procurement, and charity.

As this process moved along, comparable data for the national competitors were derived from a variety of reliable sources. Because all the firms chosen are publicly held, a wide variety of data were readily available. The majority of the data were drawn from Annual Reports to stockholders and 10K filings with the Securities and Exchange Commission. Where gaps needed to be filled, the following additional sources were consulted:

- Urban Land Institute's *Dollars and Cents of Shopping Centers: 2004*
- U.S. Economic Census
- Hoover's Online

After all data were collected, the numbers were inserted into a model developed by Civic Economics using IMPLAN multipliers for the City of Chicago. The model allows us to calculate the economic impact on the city for each business, and show it in various ways, including as a percent of revenue and per square foot of retail space. The results illustrate the differential impact of local firms and their national rivals. Because land use decisions and economic development policy are largely municipal functions, the City of Chicago was selected as the relevant jurisdiction.

The Andersonville Development Corporation also conducted a Patron Preference Survey of 512 randomly selected shoppers within the neighborhood during the month of May 2004. While this survey was not scientifically formulated, it provided detailed background information about where patrons are coming from and why they choose to shop in Andersonville.

Economic Impact Analysis

Civic Economics builds its economic impact analyses around tools and data provided by the Minnesota Implan Group, publishers of IMPLAN software and datasets. The following provides a brief description of the analysis process.

For this analysis the study aims to measure the amount of money spent on retail goods and services that remain in the local economy after consumer purchases. Therefore, Civic Economics began impact calculations not with the revenues of the firms studied but with their expenditures. Conventional application of multipliers assumes that comparable retailers have comparable impacts. The modified model utilized here follows the revenues of each business one step further to identify the actual local expenditures of that firm. This allows us to determine true economic impacts.

In this study, total economic impact is the sum of three effects: direct, indirect, and induced. The box below describes our modified methodology for using multipliers to isolate only dollars kept local.

ECONOMIC IMPACT METHODOLOGY

Direct	+	Indirect	+	Induced	=	Total
Identified spending of the business being studied		Estimated recirculation of the direct effect spending Calculated using a multiplier specific to the jurisdiction and sector				Aggregate impact of the business being studied

In this case, *direct* effects reflect the first round of local spending, such as wages and benefits, profits to local owners, local procurement, and charitable contributions. *Indirect* and *induced* effects reflect the continuing circulation of that first round of spending by businesses and individuals respectively.

Our analysis started with the direct effect spending, which was gathered from interviews with local companies and careful study of chain store corporate filings. Using this as the base, indirect and induced effects are calculated by way of multipliers, which capture the size of these effects as a ratio of total change in economic activity relative to direct effects. Multipliers provided by IMPLAN estimate indirect and induced effects and adjust for predictable leakage from the jurisdiction.

FINDINGS

The Andersonville Study of Retail Economics has produced a treasure trove of data. Civic Economics interviewed individual business owners to determine revenue and spending patterns for all ten local firms, and estimated the same data for chain businesses. To distill this massive dataset to an accessible form, we have organized it as follows:

- Aggregate Findings, including all local and all chain businesses
- Impact per $100 of Revenue, allowing a fair comparison based on consumer spending at each business
- Impact per Square Foot, allowing a fair comparison based on the space occupied by each business
- Sector Findings, grouping businesses as Restaurant, Retail, or Service

Table 1 provides a summary of key data for the analysis:

Table 1

LOCAL IMPACT SUMMARY

Local Businesses	Restaurants	Retail	Services	Total
	Star Gaze, Andies, Swedish Bakery, M Henry	Women & Children, Chicago Aquarium, White Hen	Visionary, Joel Hall, Toujours	
Total Revenue	$ 5,406,000	$ 2,310,500	$ 2,050,000	$ 9,766,500
Retail Square Footage	13500	8100	15500	37100
Revenue per Square Foot (psf)	$ 400	$ 285	$ 132	$ 263
Total Local Impact	$ 4,090,402	$ 1,005,570	$ 1,555,887	$ 6,651,859
Local Impact per $1 Revenue	0.76	0.44	0.76	0.68
Local Impact per Square Foot	$ 303	$ 124	$ 100	$ 179

Chain Businesses	Restaurants	Retail	Services	Total
	Applebees, Olive Garden, Panera, Denny's	Borders, Petco, Average C-Store	Pearle, Cinemark, Supercuts	
Total Revenue	$ 9,306,994	$ 8,962,896	$ 2,212,222	$ 20,482,112
Retail Square Footage	22330	40500	21500	84330
Revenue per Square Foot (psf)	$ 417	$ 221	$ 103	$ 243
Total Local Impact	$ 5,550,439	$ 2,392,347	$ 886,856	$ 8,829,641
Local Impact per $1 Revenue	0.60	0.27	0.40	0.43
Local Impact per Square Foot	$ 249	$ 59	$ 41	$ 105

SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

In the pages that follow, we will review this data in aggregate (all local and all chain businesses), and by sector. We cannot, however, reveal detailed data for any participating business.

Components of Local Economic Impact

The lion's share of the local economic impact of retail and service businesses is attributable to four factors: labor, profit, procurement, and charity.

Spending on local labor comprises a larger share of operating costs for a locally-owned establishment than for an outlet of a national chain. While the latter are able to consolidate administrative functions such as bookkeeping and marketing at national headquarters, independents must carry out those functions in-house or outsource within the community. Additionally, economies of scale and carefully engineered store layouts may allow national chains to employ fewer onsite staff than do locally based firms. In this study the local firms spent, on average, 29 percent of total revenue on labor costs while the national chains spent 23 percent of revenue on labor.

Secondly, a larger portion of profits earned by local ownership will remain in the local economy. Purchases of goods, services, and meals at chain outlets generate profits for the corporation, which then either reinvests in global operations or distributes a portion of profits to shareholders. In either case, chain stores profits circulating in the local economy are nominal.

Third, locally-owned businesses procure a wider array of goods and services in the local marketplace. These include goods for resale, business supplies, and professional services, among others. For the local and chain firms studied here, local procurement was roughly twice as high for local businesses (6.0 percent of total revenue) as their chain competitors (2.9 percent of total revenue).

A smaller yet significant share of the local advantage is charitable giving. The owners and employees of local firms generally live in and around their business locations and are more likely to give back to their own backyard. National firms may be more likely to donate to charities near to corporate headquarters or other large corporate facilities.

Aggregate Economic Impacts

Local impacts were first determined without making adjustments for differences in revenue and square footage. In general, the chain businesses studied draw higher total revenue and occupy larger spaces, though sales per square foot are comparable.

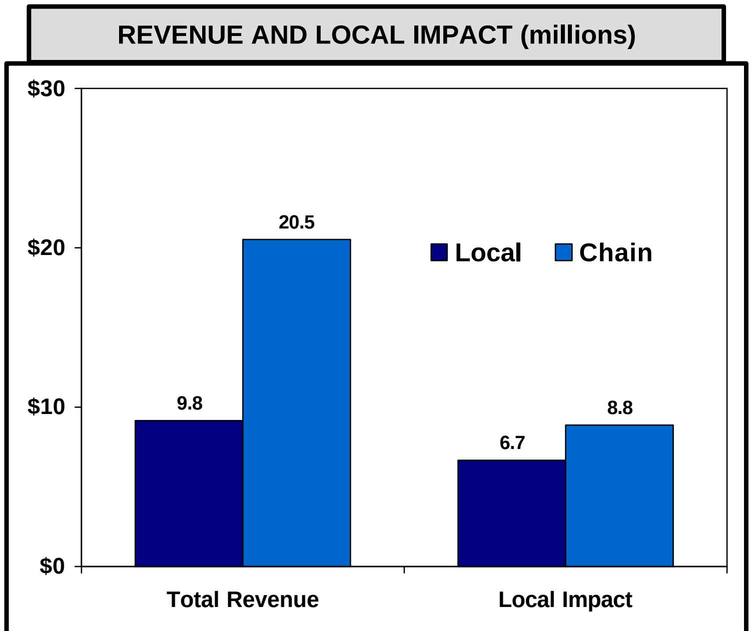
Chart 1 shows the total local economic impact of our ten local businesses and of their ten chain competitors. While the local firms generate an economic impact of $6.7 Million on revenue of $9.8 Million, the chains would generate a local economic impact of $8.8 Million on revenue of $20.5 Million.

Chart 2 provides more detail, revealing the components of the impact calculation: direct, indirect, and induced.

In this case, *direct* effects reflect the first round of local spending, such as wages and benefits. *Indirect* and *induced* effects reflect the continuing circulation of that first round of spending by both businesses and individuals. For more detail on economic impact analysis and the meaning of these components, please review the Methodology section of this document on page 10.

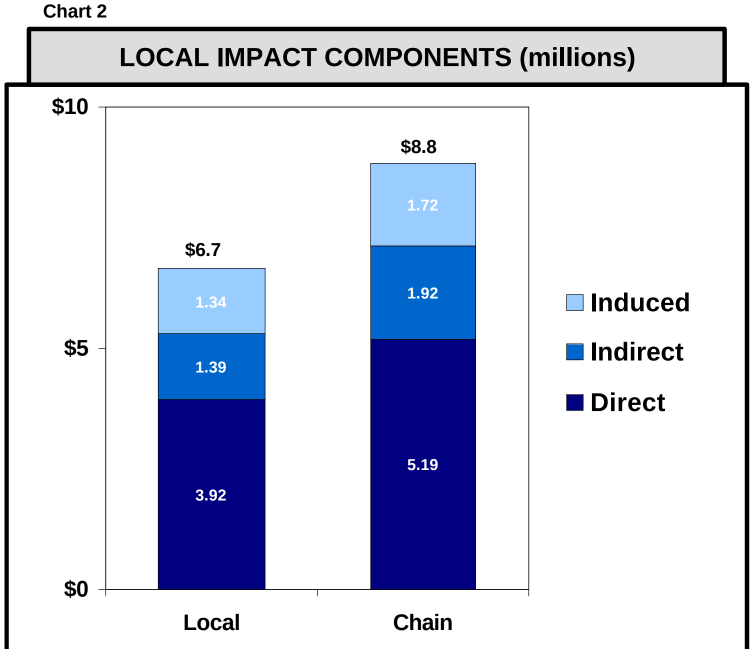
In each chart, the simplest policy conclusion jumps to the fore: these ten chain

Chart 1



SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

Chart 2



SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

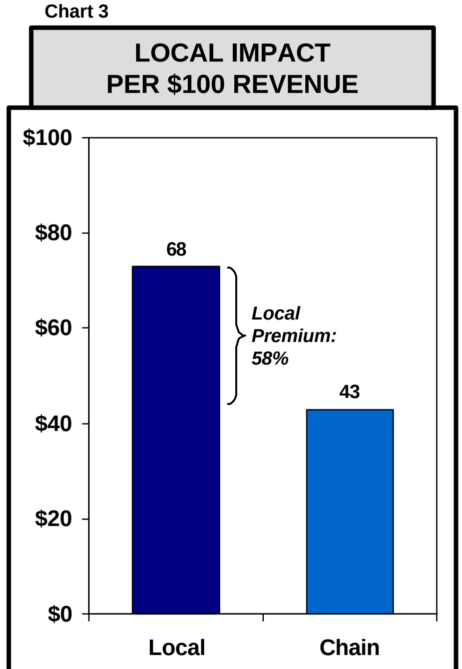
businesses create greater economic impact than the ten local firms. However, the following pages demonstrate that this simple assumption neglects to account for two essential variables: the revenue and square footage of each business. These variables, as we shall see, thoroughly erase the apparent economic impact advantage of chain businesses.

Adjusted Economic Impacts

In order to evaluate the true economic impact of any business, it must be placed in the context of the local economy, in this case the City of Chicago. Two important considerations must be added into the calculus: revenue and store size. For each factor, we have calculated a Local Premium, reflecting the additional economic impact of local firms expressed as a percentage increase over the impact of competitor chain firms.

By Revenue: Chart 3 illustrates the economic impact of local and chain businesses adjusted for total revenue, revealing that $100 in consumer spending with a mix of local businesses generates $68 in local economic impact. By contrast, the same $100 spent with competitor chains generates only $43 in local economic impact. The Local Premium in economic impact is a striking 58 percent relative to chains.

Chart 3



SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

Consumer spending in large retail markets is relatively inelastic; that is, the presence of any given business will not change total consumer spending over an extended period of time. For example, it may well be that the arrival of a new Olive Garden in a location such as Andersonville will briefly generate greater restaurant sales in the area, but it cannot be assumed that it will increase overall restaurant sales in the city. The reason for this is simple: household discretionary spending is a function of household income, not a function of choices. Because sales tax revenue is a function of retail sales activity, the chain stores studied here are largely revenue neutral in that regard.

We do recognize that certain businesses are an essential component of a city's tourist matrix, contributing to the attraction of visitors and their money. The chain businesses studied here are quite common and unlikely to generate additional sales activity in the City. On the other hand, it is clear that the unique mix of firms in Andersonville does bring shoppers from beyond the City. The Patron Preference

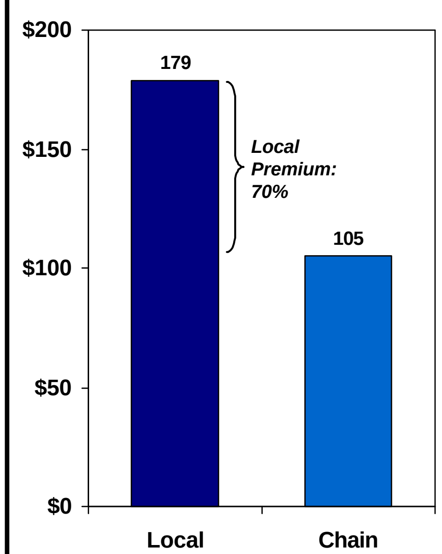
Survey conducted in coordination with this study revealed that the primary attractions of Andersonville are its mix of local businesses and traditional urban setting. The area draws spending into the city, which cannot be said of an agglomeration of common chain stores. Indeed, 10 percent of all respondents reside outside the City of Chicago.

By Size: Chart 4 illustrates the economic impact of local and chain businesses adjusted for total square footage. For every square foot occupied by local businesses, the economic impact in the City of Chicago reaches $179. By contrast, for every square foot occupied by chains, the economic impact reaches only $105. The Local Premium is a striking 70 percent relative to the chains.

The chain firms studied here occupy spaces twice as large as their local competitors. They also achieve total sales roughly twice as high. Local and chain businesses in the study attain comparable sales per square foot, $263 for locals and $243 for chains. This figure will surprise many, and it is of significance in evaluating the economic impact of chains.

Chart 4

LOCAL IMPACT PER SQUARE FOOT



SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

Urban policy makers pay close attention to real estate occupancy and absorption rates, as improvements in these measures reflect the health of the local real estate market. National chains are often believed to improve these measures, if only because they occupy more space per outlet. Returning to the example of the typical Olive Garden, on opening day the restaurant has occupied 8,200 square feet of space. However, if the revenue to support that square footage is merely diverted from other businesses in the area, its impact on occupancy and absorption will be negated over time.

So, where policy makers might be tempted by the aggregate impacts outlined above, adjustments for revenue and size dispel the notion that chains will generate greater sales tax revenue or more effectively utilize the city's real estate. The gradual replacement of local firms with chain competitors instead produces serious negative consequences, denying the community and its citizens the benefits of the Local Premium.

Economic Impacts by Sector

Given the variety of businesses participating in this study, Civic Economics was given a unique opportunity to see how outcomes differ by the nature of the business. In this case, we have sorted firms into three sectors: Restaurant, Retail, and Services.

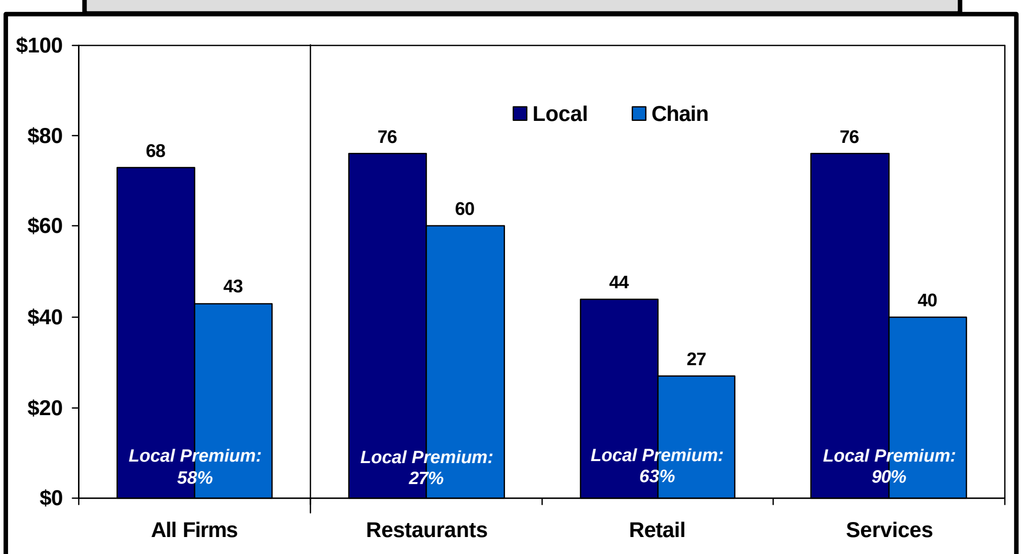
- Local restaurants include Star Gaze, Andies, Swedish Bakery, and M Henry; competitors include Applebee's, Olive Garden, Panera Bread, and Denny's.
- Local retailers include Women and Children First, Chicago Aquarium and Pond, and White Hen; competitors include Borders, Petco, and a hypothetical company-owned convenience store.
- Local service providers include Visionary Eye Care, Joel Hall Dancers, and Toujours Spa and Salon; competitors include Pearle Vision, Cinemark, and Supercuts.

As with the analyses above, we adjusted these impact analyses to account for variations in revenue and square footage. The aggregate Local Premium is substantial, whether adjustment is made for revenue or size; however, these variables play out quite differently when the data is broken out by sector.

Chart 5 illustrates the economic impact per $100 of revenue across the three sectors.

Chart 5

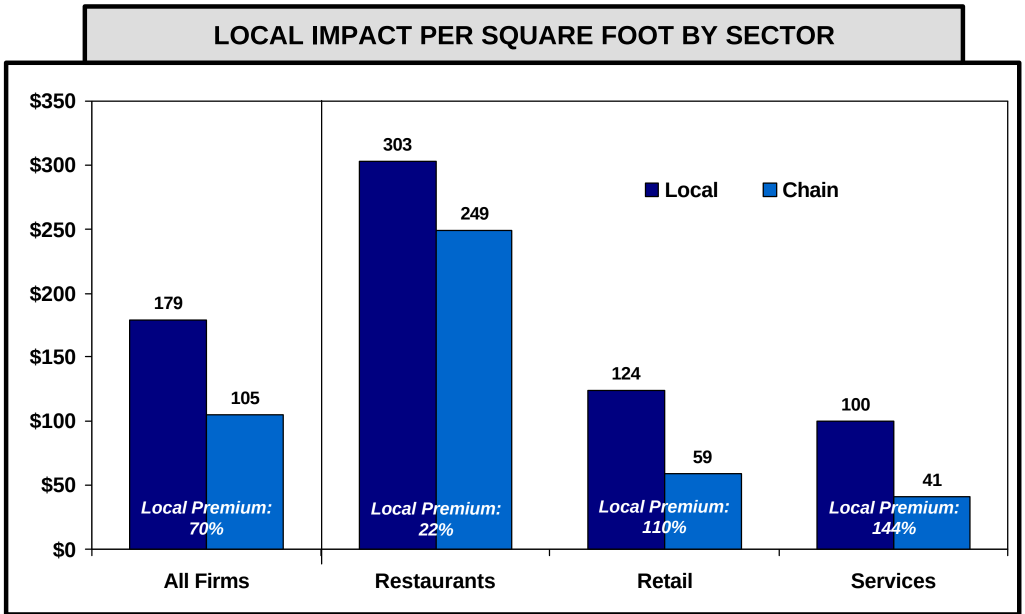
LOCAL IMPACT PER $100 REVENUE BY SECTOR



SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

Chart 6 illustrates the economic impact per square foot across the three sectors.

Chart 6



SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

Much of the difference in impact among the sectors is accounted for by labor costs. Moreover, these costs are heavily localized, as employees and proprietors are drawn largely from within the City of Chicago.

Among restaurants, for example, labor costs ranged from 20 percent of total revenue to 43 percent of total revenue. Labor costs at local restaurants averaged 28 percent, kept low by two operations in which owners provide substantial labor while taking little in wages and profits. At chains, labor costs averaged 34 percent, though only one operator, Denny's, exceeded the average, reporting a surprising 43 percent.

Service providers, perhaps predictably, expend a large portion of revenues on labor. However, the data make clear that locally-owned firms expend a much larger portion on labor, including both employees and proprietors. Indeed, though we did not evaluate wage and benefit rates for individual employees, it appears that the presence of an owner is a significant factor in the extraordinary Local Premium among service firms

One last area of analysis was the impact of a locally-owned franchise in comparison to a wholly corporate-owned and operated chain store. In this case the locally franchised White Hen Pantry mirrored a nationally owned chain store in most expenditure categories with the major difference being that bottom line profit for the franchisee remained in the community. This provided a Local Premium for the locally-owned franchise, albeit much slimmer than the other locally-owned businesses present over their competitors.

POLICY IMPLICATIONS

With so much data collected for the Andersonville Study, we are certain that interpretation will continue long after its release. However, several significant policy implications should be noted here.

Creativity, Opportunity, and Prosperity

Civic Economics is dedicated to the pursuit of those attributes in client communities. The findings of this study demonstrate strongly that the Andersonville model (diverse offerings, human scale, locally-owned businesses) is far superior to the increasingly common suburban model (consolidated offerings, auto scale, chain businesses) in promoting those attributes.

In the age of the mobile "creative class," American communities seek to promote and celebrate their unique attributes. Chicago has led the way in celebrating cultural diversity, neighborhood vitality, and a distinctly midwestern urbanism. These are the very attributes on display in Andersonville and those most directly threatened by the proliferation of chain businesses.

ANDERSONVILLE'S CLARK STREET

SOURCE: Terraserver USA, US Geological Service

Civic Economics made no attempt in this study to evaluate wages and benefits. However, we can say with certainty that the Andersonville model of diverse local firms provides an opportunity for entrepreneurship severely constrained by chain proliferation. As yesterday's proprietors become tomorrow's employees, there can be little doubt that something has been lost.

The findings of this study make quite clear that local firms contribute mightily to local prosperity in comparison their chain competitors. The Local Premium identified above is a real and quantifiable demonstration of the drainage of dollars from the community by chain businesses.

Neither Civic Economics nor its Andersonville clients will argue that chain firms have no place in the city. Fair market competition plays an essential role in any economy, and consumer preferences must be respected. However, policy makers must ensure that the playing field is level, that local firms are not inadvertently disadvantaged by faulty premises or unintended consequences.

Urban Redevelopment and Chain Retail

Like other major cities adjusting to new economic realities, Chicago faces the monumental challenge of redeveloping obsolete and blighted sites. The city has achieved unparalleled success in doing so. Across the city, new and rehabilitated buildings provide appealing and accessible options in the spirit of New Urbanism, filling gaps in the urban fabric and in municipal revenues. Chicago has pioneered an array of planning and development tools to achieve this success, providing public support and incentives for redevelopment projects.

However, any tour of such sites will reveal a troubling fact: chain outlets anchor many redevelopment sites. As a result, these projects introduce new, often publicly subsidized, competition to local businesses. As demonstrated in this study, that unbalanced competition siphons dollars and economic vitality from the community as consumers move spending from locals to chains.

During BookExpo 2004, held in Chicago, Civic Economics led a discussion of this phenomenon with America's leading independent booksellers. They reported common experiences from Miami to Seattle.

Developers of these sites share an urban vision of lively, pedestrian-friendly neighborhoods. Architectural renderings depict bookstores, restaurants, and coffee shops with distinctive local flourishes. Municipalities offer a variety of incentives to make the vision a reality. However, the reality often diverges in substantial ways as developers follow conventional leasing strategies, signing chain stores and formula restaurants to the most prominent storefronts. From these privileged locations, subsidized chains gain a competitive advantage over nearby independents.

We believe that cities can capture all of the advantages of redevelopment without inadvertently harming local merchants. Incentive conditions and development guidelines can promote the placement of unique local businesses in new projects. Risk to the developer can be reduced through lease guarantees or low interest financing with minimal exposure to the city. Modest changes in planning and development practice will allow the continued revitalization of Chicago without diluting the city's unique character or foregoing the Local Premium provided by local firms.

Public Revenue and Economic Development

Policy makers rightfully seek to maximize public revenues without raising tax rates, and often proceed on the assumption that attracting local outlets of national chains will do that. However, the findings above demonstrate that their arrival is, at best, revenue-neutral even in the near term. Moreover, the inevitable long-term consequence of forgoing the Local Premium identified above is a gradual decrease in public revenues, as those dollars are no longer available to generate taxable transactions within the city.

Economic development policy did not focus on chain businesses until the recent economic downturn. Faced with a dearth of factory and headquarters prospects, practitioners found their best prospects in chain stores and restaurants and have portrayed these as economic development “wins.” As it must often do, Chicago can lead the way in repudiating this counterproductive approach to economic development.

Factories or corporate headquarters, which produce goods and services for export, drawing dollars into the community and clearly enhancing the local economy and tax base, are the legitimate and traditional targets of economic development policy.

Stores, restaurants, and service providers, by contrast, produce goods and services for local consumption. In general, the dollars that enter these businesses are the dollars of Chicagoans. Therefore, the appropriate measure is not how much revenue any outlet earns but rather how much of that revenue it shares with the community rather than siphons from it. The findings of this study make clear that economic development goals are actually hindered when chain businesses receive preferential treatment.

We do recognize that certain chain stores and restaurants are an essential component of a city’s tourist matrix, contributing to the attraction of visitors and their money. However, those firms are exceptional and in no case can the chain firms studied here be recognized as tourist draws. In fact, as the Patron Preference Survey demonstrates, it is traditional business districts like Andersonville that provide Chicago an edge in attracting visitors and their spending.

Urban Design Considerations

Chicago’s distinct urban character is on display on Clark Street in Andersonville. Buildings are scaled to pedestrians and present a street wall that is varied yet harmonious. These buildings provide relatively small spaces for hundreds of retailers, restaurants, and service providers. Patrons are pulled along the street by diverse shop windows and signage.

If chain competitors supplanted the local businesses of Andersonville, that streetscape would be dramatically and adversely affected. The chains studied here average twice the square footage of the locals. Shop windows, entrances, and signs would thus be stretched twice as far apart. Small structures that have served the neighborhood for decades would be rendered obsolete, either abandoned or replaced by larger formulaic structures.

Perhaps more importantly, Andersonville shares these attributes with dozens of neighborhoods throughout the city, all of which are similarly under assault. While generic agglomerations of chain stores are widely available throughout the metropolitan area, these traditional urban districts offer a distinct character that cannot be replicated.

The Customer Preference Survey conducted by the Andersonville Development Corporation highlights this distinction. When asked to express a preference on the type of business shoppers choose to patronize, over 70 percent chose locally-owned businesses while less than three percent chose chain businesses. Additionally, an overwhelming 80 percent of respondents identified Andersonville's traditional neighborhood district as their preferred shopping environment.

These results back up the belief in the neighborhood that Andersonville's unique businesses and layout are a draw, attracting people from both inside and outside the region. Indeed, among survey respondents, over 10% were from outside the City of Chicago. Districts such as Andersonville provide the City with a unique advantage, drawing patrons from throughout the region and offering tourists an experience they are unlikely to find at home.

The Economic Impact of Consumer Choices

The Andersonville Study was crafted to provide policy makers with the information they need for rational decision-making. However, we would be remiss if we failed to address another critical audience with the power to make a substantial difference in the economic health of Chicago: consumers.

From a bottle of soda to a night on the town, from books and fish to eye care and dance lessons, the businesses studied here offer a range of goods and services that ordinary Chicagoans purchase every day. With each purchase, consumers put into play their hard earned dollars; the consumer's decision to patronize a local firm versus a chain competitor ripples through the economy with dramatic results.

The ten local firms participating in this study generate nearly $10 Million in revenue each year. Of that sum, roughly $6.8 million remains in Chicago. Were consumers to abandon these firms and direct that $10 million in spending to their chain competitors, only $4.3 million would remain. The missing millions would have flown off to corporate offices outside the region. Once siphoned away, that money cannot go to employ Chicagoans, to improve Chicago homes, or to support Chicago churches and charities.

In one of the largest urban economies in the nation, these few million dollars may seem insignificant. Yet it must be remembered that we have studied here only ten small businesses in one Chicago neighborhood. The $10 Million in revenue we followed here is but a drop in the city's total sales of goods and services, which is measured in the tens of billions.

While we cannot make claims about the applicability of these exact figures beyond the businesses studied here, it is clear that the purchasing decisions of Chicago consumers determine the fate of billions of dollars. Whether that money stays or goes is dependent upon the individual shopping choices of individual consumers.

The Bottom Line

Andersonville is a model for prosperous communities nationwide. There, Chicagoans offer a wide array of products and services, keep local dollars in the local economy, and contribute to Chicago's privileged place among American cities. But Andersonville and the dozens of neighborhoods like it are particularly threatened by the proliferation of chain businesses.

Public policy in Chicago must seek to protect and promote the Andersonville model rather than facilitate its demise. Indeed, it may be in the best interests of communities to institute policies that directly incentivize them.

ABOUT THE STUDY

About Andersonville

Andersonville is a distinctive neighborhood on the north side of Chicago. Locally-owned businesses have been a primary element in its success throughout its history. First established as a farming community in the 1850s, the retail district began as an enclave of small businesses when Swedes moved north to escape the neighborhoods that had been ravaged by the Great Chicago Fire in 1871. The residential community remained primarily Swedish for decades, until, like many established groups, the Swedes began migrating to the suburbs in the 1950s.

In 1964, the small business owners banded together to organize a huge parade, led by Mayor Richard J. Daley, in a celebration to rededicate the neighborhood to its Swedish roots. In the mid-1980s, the neighborhood was experiencing disinvestment in the commercial district. The business owners again organized, with the help of locally-owned banks, and provided financing for new start-ups to revitalize the district, as well as community-wide marketing. The combined efforts drew key new local enterprises onto Clark Street, and with them came renewed interest in Andersonville's residential areas.

Today, Andersonville is one of Chicago's most popular neighborhoods. It is still considered one of the most concentrated areas of Swedish culture in the United States and is home to the renowned Swedish American Museum. In addition, Andersonville hosts a diverse assortment of devoted residents and businesses, including one of Chicago's largest gay & lesbian communities, a large collection of Middle Eastern restaurants and bakeries, and a thriving Hispanic commercial area on its north end.

Discover the small-town charm of Chicago's Andersonville neighborhood. A great place to start is the website of the Andersonville Chamber of Commerce, *www.Andersonville.org*.

About Civic Economics

Civic Economics is an economic analysis and strategic planning consultancy with offices in Austin and Chicago. Since its founding in 2002, the firm has established itself as a leader in progressive economic development, taking its unique vision of sustainable prosperity across the USA and Mexico.

More importantly, the firm has emerged at the center of a network of planners and independent businesses promoting reasoned analysis of the evolving American retail scene. We've provided information and counsel to dozens of civic organizations in the USA and Canada. Our observations have appeared in news outlets from New York Times to San Diego. We have developed an unmatched understanding of the dynamics of local retail and service provision, a library of best practices information, and a network of contacts from business, government, and civic organizations nationwide.

Learn more about the firm and "*The Civic Economics of Retail*" by visiting us online at www.*CivicEconomics.com*.

Participating Firms

Andies Restaurant is a family owned restaurant serving Mediterranean, Lebanese, and Greek foods. Owner Andie Tamras has been serving Andersonville residents and visitors for 30 years. He participates in many local fundraisers and enjoys being a community destination for many holiday meals.

The Chicago Aquarium and Pond Company meets all the needs of the pond and aquarium hobbyist. It was started back in 1981 and owners Harold Ellis and Ken Riley have lived above their shop since 1988. As such, they are invested in Andersonville in both their professional and personal spheres.

The Joel Hall Dancers and Center was founded in 1974 by Joel Hall and Joseph Ehrenberg. Offering over 150 weekly classes for dancers of all ages, the studio reaches out to those who would not otherwise be exposed to the arts for classes, educational outreach programs and performances.

M Henry is a recent addition to the Andersonville scene. This restaurant features a breakfast and brunch menu that puts a modern spin on some classic dishes. Owner Michael Moorman chose a location at the northern end of the neighborhood, expanding the geographic diversity in Andersonville.

Star Gaze is a restaurant and bar catering primarily to the neighborhood's lesbian population. The community minded owners donate time and space to many nonprofit organizations that cannot afford those expenses.

Swedish Bakery is the ultimate neighborhood sweet shop. Traditional Swedish products are featured, as well as a selection of other European and old fashioned American items. An expansion in 1989 tripled the size of the Swedish Bakery, raising employment from 19 to its current 55 employees.

Toujours Spa and Salon is another recent addition to Andersonville. This upscale salon and spa provides a service more commonly found downtown. The quality of work provides residents of Andersonville an amenity they once had to travel outside the neighborhood to enjoy.

Visionary Eye Care is a full service eye care facility, providing a unique health service and a full range of stylish eyewear. Drs. Michael Ciszek and Barbara Butler-Schneider and all their employees live in Andersonville.

White Hen Pantry is the locally-owned outlet of a well-known convenience store franchisor. Owner Cecilia Lemus was an employee at the store before recently purchasing the franchise rights.

Women and Children First is one of the largest feminist bookstores in the country, with over 30,000 books, and plays host to many book signings and events from local, regional, and national figures. Co-owner Ann Christopherson has been a vocal proponent of independent bookstores and retailers throughout the country and has recently served as President of the American Booksellers Association.

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To learn more about the Andersonville and to obtain copies of study documents, please visit *www.AndersonvilleStudy.com*.

The SAN FRANCISCO RETAIL DIVERSITY STUDY

SFLOMA

CIVIC ECONOMICS
CREATIVITY · OPPORTUNITY · PROSPERITY

MAY 1, 2007

www.CivicEconomics.com/SF

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INTRODUCTION

Civic Economics is pleased to present the San Francisco Locally Owned Merchants Alliance with this study of the health, diversity, and economic impact of independent merchants in San Francisco. The Northern California Independent Booksellers Association provided oversight for this study in the person of Executive Director Hut Landon.

Research Background

Austin In late 2002, shortly after Civic Economics was formed to provide strategic planning and analysis services to the economic development community, Austin, Texas was engaged in a rousing fight about chain retail in the expanding downtown area. The corner of Sixth and Lamar was the longtime home of two retailers that had earned a place among Austin institutions, BookPeople and Waterloo Records. A retail development at the intersection had been awarded City of Austin incentives through a variety of channels with a total estimated value of just over $2 Million. Enthusiasm was high until the developer announced that the anchor tenant was to be Borders Books and Music, effectively setting up a subsidized chain competitor directly across the street from established local firms.

As is often the case with large format retailers in urban settings, the debate was driven by the emotional appeal to “Keep Austin Weird.” At Civic Economics, we conceived a methodology for quantifying the true economic impacts of the proposed development and shared the idea, unsolicited, with the owners of BookPeople and Waterloo. Within days, work was underway on the study, with funding provided by the fledgling Austin Independent Business Alliance and Liveable City.

Civic Economics reviewed the financial records at BookPeople and Waterloo to identify the portion of total store revenue that recirculated in Austin in such areas as labor costs (including locally retained profits), local procurement of goods (for internal use and for resale) and services (attorneys, accountants, etc.), and charitable giving. Without direct access to Borders in-store accounting, we turned to public filings to identify line items attributable to local operations. Where precise allocations could not be made (for example, the proportion of labor costs associated with headquarters operations or the distribution of corporate charitable contributions), we chose in every case to err on the side of the company, assuming the greatest local spending fiscally possible.

While we anticipated that the local retailers would recirculate somewhat more money in the Austin area than Borders, we were taken aback at the dramatic difference. Indeed, the findings were so startling, we returned to the merchants to double check our figures and turned to two respected professors at the University of Texas for further review our work. Upon completion, the final figures were as follows (chart at right):

Austin Impact Findings, 2002

When the study was released in December of 2002, it not only turned the debate decidedly in opposition to the Borders subsidies, the substantial media coverage drove increased holiday sales at BookPeople, Waterloo, and a host of Austin independents. For a variety of reasons, Borders ultimately withdrew from the site, which later became the headquarters and flagship store for Whole Foods. However, as the $45-to-$13 impact figure began circulating around the nation, Civic Economics was concerned that the specific finding from a very small and exceptional sample was unlikely to reflect the economic realities of other communities or other merchants with different lines of goods and services.

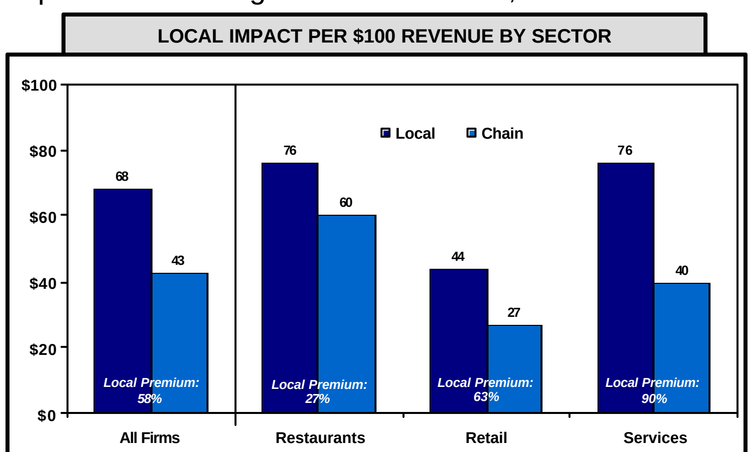
Chicago We began searching for another opportunity to conduct a broader study, and found it in Andersonville, a diverse, urban neighborhood in the City of Chicago (which was, coincidentally, where Civic Economics' Matt Cunningham had recently relocated).

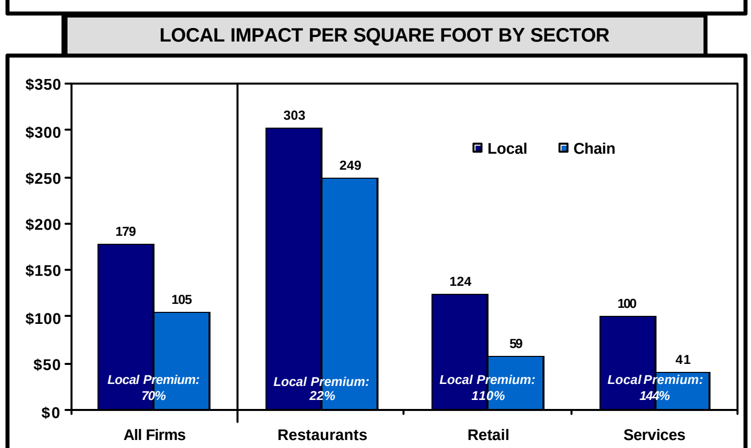
The Andersonville Chamber of Commerce worked with Civic Economics to recruit ten independent business participants to the study: four restaurants, three retailers, and three service providers. For comparative analysis, a publicly-held chain competitor was identified for each local business. Then, Civic Economics refined and applied the Austin methodology, taking full advantage of the far greater dataset available to us.

For both locals and chains, local economic impact was quantified, again including such things as local labor costs, local procurement of goods and services, local retention of profits, and charitable giving. In other words, the analysis quantified the portion of the retail dollar remaining in local circulation after the retail transaction.

The difference between these impacts, which were now labeled the Local Premium, were calculated for all firms and by business type. In addition, Civic Economics collected information about store size in order to calculate impacts by square foot, a useful bit of information in built-out urban areas.

Again, the results were striking, reinforcing the notion that local firms of all types recirculate substantially more money within the community than their chain competitors.





SOURCES: Interviews with all local businesses, Annual Reports for all chain businesses, Minnesota Implan Group, Urban Land Institute *Dollars and Cents of Shopping Centers* 2004, Civic Economics.

As in Austin, the study drew extensive attention to the value of independent business and the importance of public policies that avoid inadvertently favoring chain competitors.

Since the release of the Andersonville Study of Retail Economics, Civic Economics has had the opportunity to review regional retail economics in a variety of settings. Speaking and consulting engagements have provided the opportunity to look at the health of independent businesses communities from Santa Cruz to the Hamptons and from Alaska to the post-Katrina Gulf Coast. One recurring and unanswered question involved the local market share of independent businesses. In two studies, though, Civic Economics had been able to estimate market share in specific retail sectors in small communities, and it became clear that the methodology could be scaled up, providing for the first time a clear and credible understanding of how independents were faring in a large market.

The San Francisco Study

This study is the culmination of two years of discussions with SFLOMA. During that time, our organizations worked together to craft a study worthy of the tremendous diversity and vitality of the locally-owned merchants in San Francisco, not one that simply repeats earlier studies.

Initially, we were faced with the issue of defining a workable study area out of the massive and diverse Bay Area. Because SFLOMA members are concentrated in the City of San Francisco proper, the city became the core of the study area. After discussion of suburban areas convenient to the city, three jurisdictions (defined in this case by ZIP Code) were included in the study: Daly City (94015), Colma (94014), and South San Francisco (94080). These communities are adjacent to and just south of the city and offer shoppers an array of choices, featuring a variety of big box and specialty chain retailers.

SAN FRANCISCO RETAIL DIVERSITY STUDY AREA

Secondly, Civic Economics and SFLOMA identified several lines of goods for consideration, with a goal of selecting five for further study. Ultimately, the lines of goods selected for study were Books, Sporting Goods, Toys, Limited Service Dining, and Hardware. Each of these lines of goods offered a strong but limited number of chain competitors as well as a healthy group of independent merchants in the region.

STEPS IN THE SAN FRANCISCO RETAIL DIVERSITY ANALYSIS		
1 Estimate market share of independent businesses in each line of goods	2 Calculate economic impact of independent businesses	3 Forecast enhanced impacts associated with redirected consumer spending

The first line of inquiry was to develop estimates of the market share captured by independent merchants in each line of goods. Over the years, we have heard that question repeatedly, and the questioner typically assumes there exists a dataset from which the answer can be extracted. In small market studies of specific issues, Civic Economics had developed market share estimates for a variety of merchants, but the process required a labor-intensive review of all competitors. The methodology utilized here represents a scaling-up of that review and the incorporation of additional sales that take place in big box, general merchandise stores, and, where it represents a substantial portion of sales, online.

Secondly, Civic Economics applied the detailed local economic impact findings from the Andersonville Study of Retail Economics to these local and chain market shares to determine the broad economic impact of each. Local merchants, as demonstrated in our prior work, recirculate substantially more revenue in a regional economy than do their chain competitors, and the impact of that recirculation can be credibly measured.

Finally, this study attempts to provide consumers and policy makers with an understanding of the economic benefits of redirecting spending from chains to independents. Starting with the economic impacts described above, we forecast economic output and employment gains that may be expected if consumers make modest changes in their shopping and dining habits and if policymakers avoid inadvertently disadvantaging small firms.

1 Estimate market share of independent businesses in each line of goods

MARKET SHARE ANALYSIS

In two previous studies, Civic Economics was retained to forecast the economic impact of so-called supercenter retailers proposed in small communities with relatively well-defined market areas. In those cases, we undertook an analysis of current market shares in those lines of goods likely to be significantly altered by the opening of the proposed supercenter.

Civic Economics frequently draws upon retail sales data provided by Claritas, "the pre-eminent source of accurate, up-to-date demographic data and target marketing information about the population, consumer behavior, consumer spending, households and businesses within any specific geographic market area in the United States." This database provides the most credible estimates of total retail spending on specific lines of goods and services within a user-defined market area. In small markets, then, the process of estimating market share is a manageable task of allocating those sales to existing merchants. In one case, the municipality provided actual sales records to facilitate the analysis. Scaled up, however, this methodology presents challenges, as the total number of businesses to account can grow quickly as the market expands.

In selecting lines of goods for this study, the number of chain competitors likely to be present was one significant factor. Upon preliminary review, for example, we eliminated women's clothing from the analysis due simply to the vast number of chain stores offering or featuring that line of goods. In the five lines selected for study, the chain competitors were both limited in number and largely publicly held, allowing a somewhat labor-intensive but achievable analysis. Even limited service dining, with literally hundreds of competitors in fast food restaurants, sandwich shops, and coffee houses, could be credibly quantified with data provided by QSR Magazine, a trade journal for the quick service restaurant industry.

Market Share Methodology

After a review of several lines of goods and services for inclusion in the study, SFLOMA and Civic Economics settled on the following:

CHAIN RETAILERS INCLUDED IN THE ANALYSIS (# of study area stores, 2005)

Booksellers	Sporting Goods Stores	Toy Stores
Borders (3)	Sports Authority (1)	Toys 'R Us (4)
Barnes & Noble (2)	REI (1)	Disney Stores (3)
B. Dalton (1)	Golfsmith (1)	-----
Waldenbooks (1)	Big 5 (1)	Target (2)
-----	Copeland (1)	Costco (2)
Target (2)	-----	
Costco (2)	Target (2)	
	Costco (2)	

Limited Service Dining Outlets

Arby's (2)	Einstein/Noah's Bagels (9)	Peet's (18)
Baja Fresh (1)	Fuddrucker's (1)	Pizza Hut (5)
Baskin-Robbins (4)	Great Steak & Potato (2)	Popeyes (4)
Boston Market (2)	In-N-Out Burger (2)	Quiznos Subs (15)
Burger King (16)	Jack in the Box (8)	Sbarro (2)
Carl's Jr.2 (5)	KFC (15)	Seattle's Best (3)
Chipotle (1)	Little Caesars Pizza (1)	Starbucks (85)
Cold Stone Creamery (2)	McDonald's (26)	Subway (39)
Del Taco (1)	Panda Express (5)	Taco Bell (15)
Domino's Pizza (1)		Wendy's (2)

In addition, we set out to study competition in the line of goods best categorized as Hardware. That sector was appealing because it has faced rapid change over the last decade as Home Depot and Lowe's have entered every market of any size in the nation, often co-locating within sight of one another. However, as we discuss further below, the novel practices of these home improvement warehouse chains has, for the time being, confounded our ability to quantify market shares for retail activity because wholesale and retail sales are increasingly intermingled.

For the remaining four sectors, though, Civic Economics undertook a labor-intensive but rather straightforward analysis, depicted on the following page.

MARKET SHARE CALCULATIONS

CALCULATING SALES AT INDEPENDENT LOCAL MERCHANTS

	Local Retail Sales for Line of Goods at Specialty Stores	*Source: Claritas*
-	Local Retail Sales at Specialty Chain Merchants	*Source: Analysis of Public Filings and Trade Journals*
=	**Local Retail Sales Remaining to Independent Merchants**	

CALCULATING TOTAL SALES FOR LINE OF GOODS

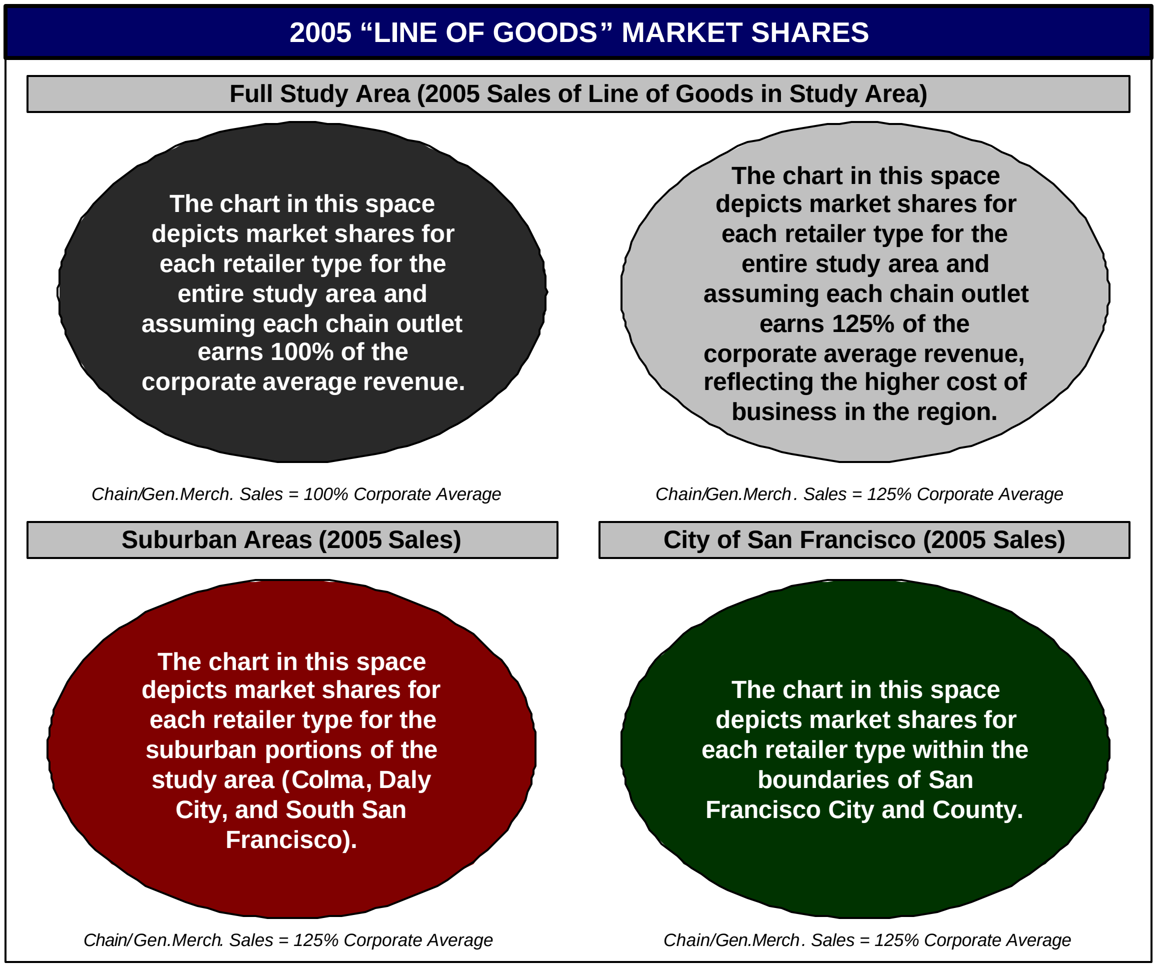
	Local Retail Sales for Line of Goods at Specialty Stores	*Source: Claritas*
+	Local Retail Sales for Line of Goods at General Merchandise Stores	*Source: Analysis of Public Filings and Trade Journals*
+	Local Sales for Line of Goods at Major Online Merchants	*Source: Analysis of Public Filings and Trade Journals*
=	**Total Local Sales for Line of Goods**	

CALCULATING MARKET SHARE FOR EACH MERCHANT TYPE (Specialty Chain, Independent, General Merchandise, Online, Other)

$$\frac{\text{Local Sales for Line of Goods for Merchant Type}}{\div \; \text{Total Local Sales for Line of Goods}} = \textbf{Merchant Type Market Share}$$

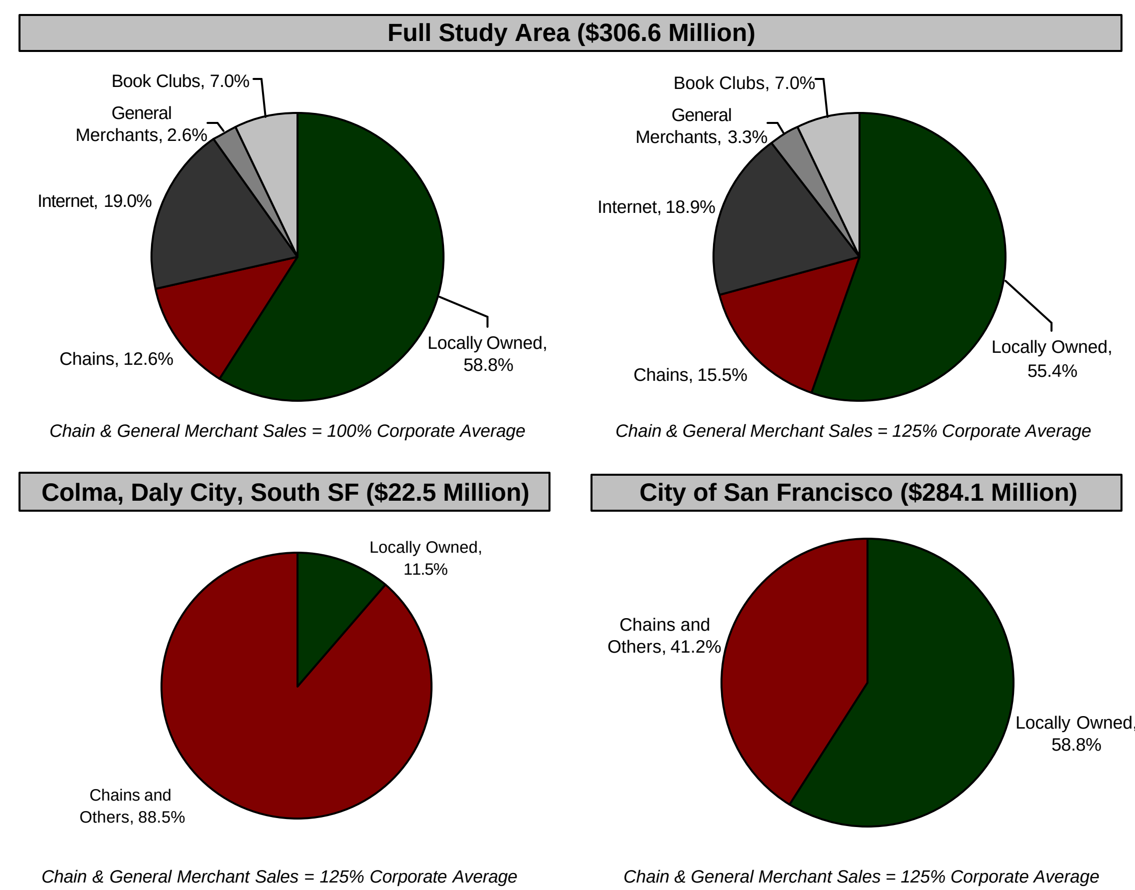
Market Share Findings

On the pages that follow, 2005 market shares for a variety of retailer types and variables are presented in a graphic format. The charts are laid out as follows:

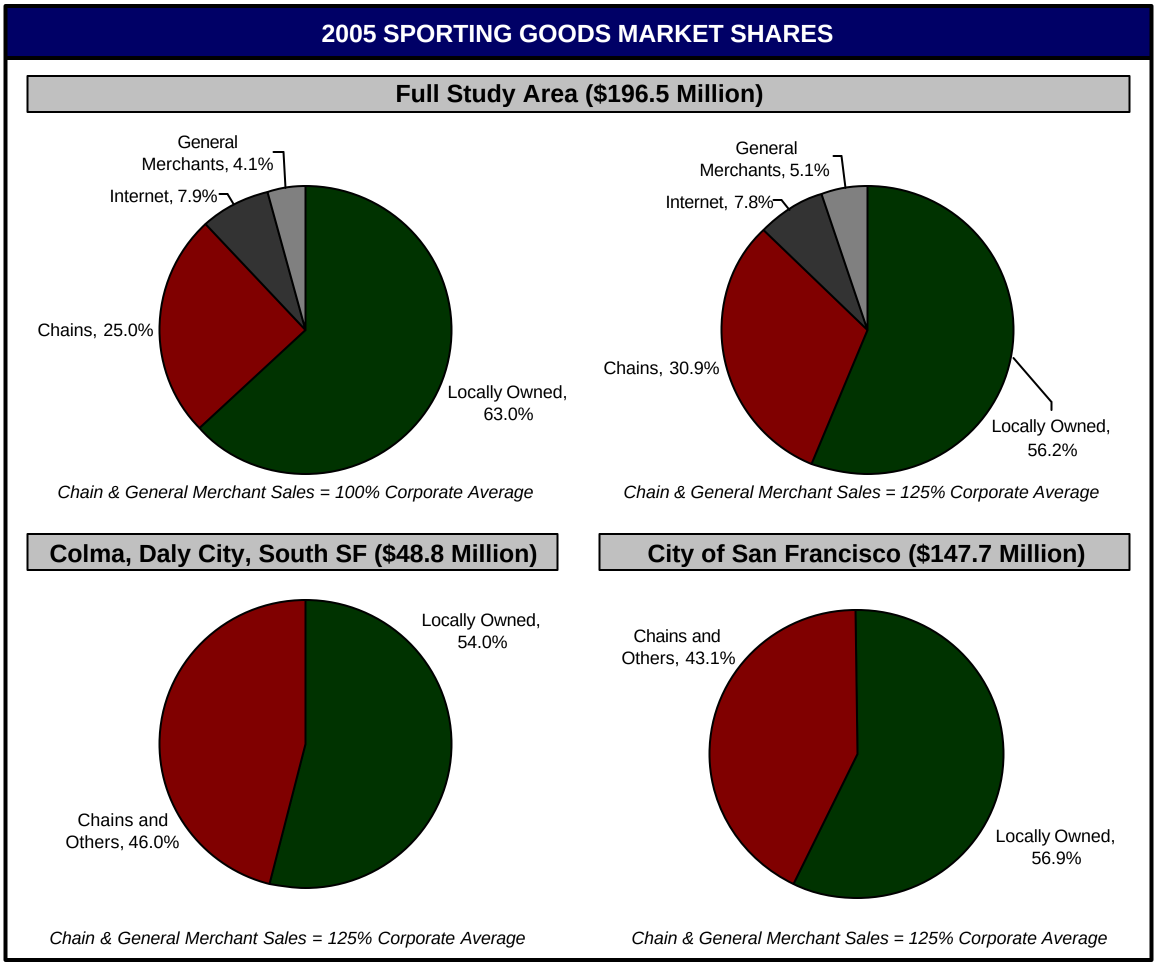


- Each chart is followed by brief explanatory notes.

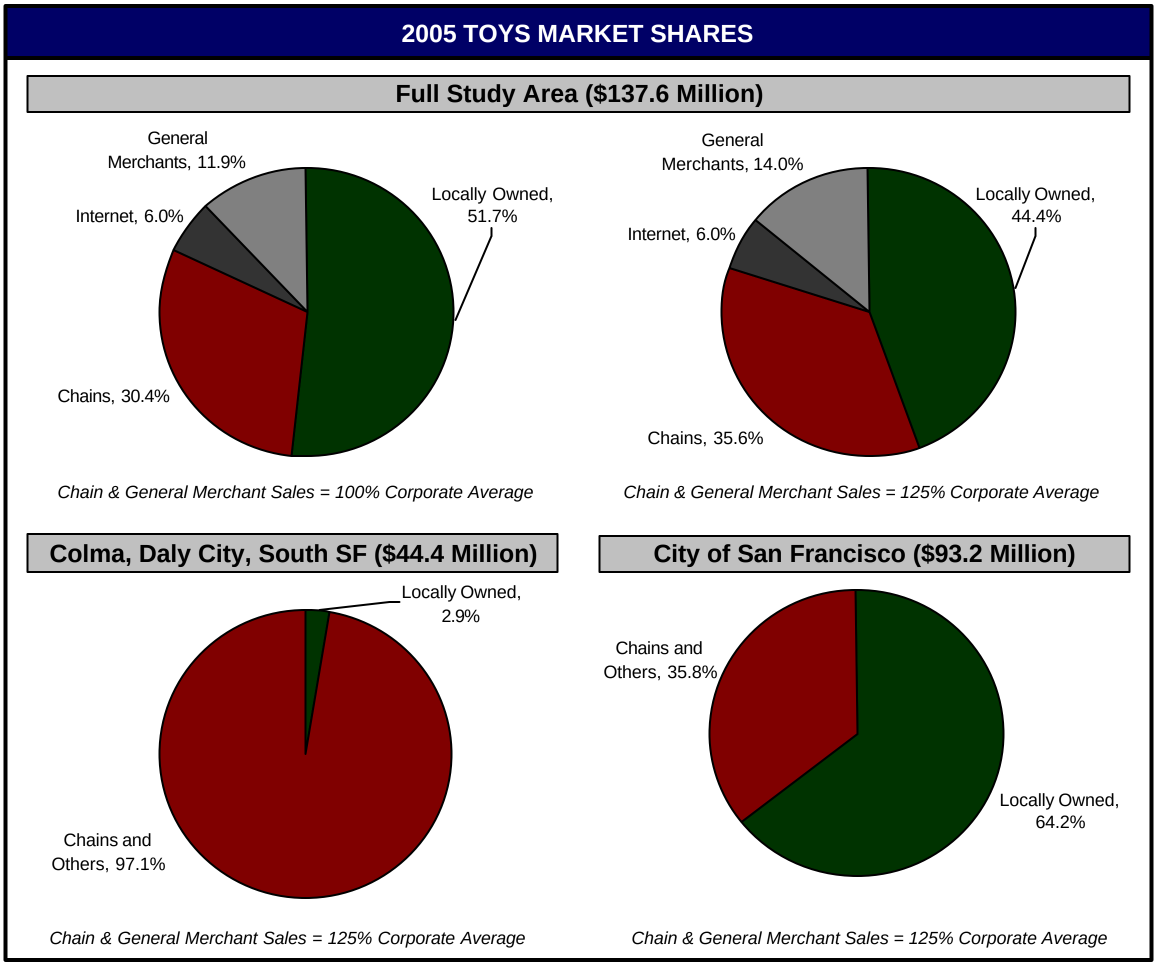
2005 BOOKSELLER MARKET SHARES



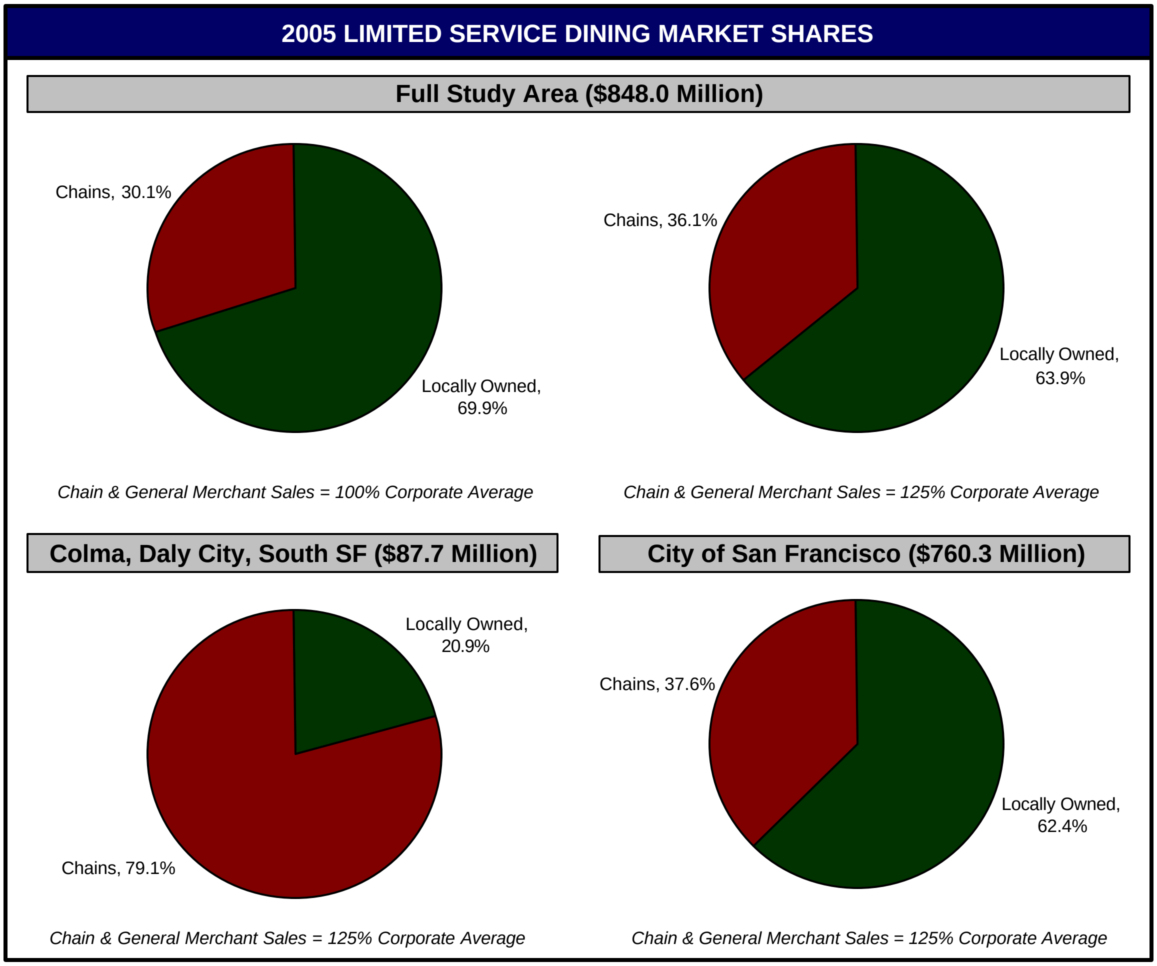
- As a portion of book sales at businesses primarily engaged in bookselling, Internet sales at Amazon.com and BandN.com are generally estimated at 21%. The reduced market share in the charts above results from the inclusion of book sales at general merchandise stores and through book clubs.
- San Francisco area independent booksellers capture an unusually high market share; the national market share for independents is currently less than 10%, according to Ipsos BookTrends.
- Barnes & Noble and Borders have each made modest inroads into the City of San Francisco. Urban expansion of large-format book chains has been easier than for other lines of goods due to the smaller footprint of the stores.
- Sales totals for this category includes conventional bookstores as well as religious booksellers, comic and fantasy shops, newsstands, and college bookstores (the last of which may account for substantial sales, with national averages of $720 per student according to the Association of College Stores).
- Average Target stores are estimated to achieve approximately $1 Million per year in book sales: Average Costco stores are estimated to achieve approximately $2 Million per year in book sales.



- The chain sporting goods segment remains in a state of flux, with a number of corporate restructurings in recent years, the dominant regional chains in San Francisco are Sports Authority and REI, with smaller shares held by the small-format Golfsmith and Big 5 chains.
- Average Target stores are estimated to achieve approximately $1 Million per year in sporting goods sales: Average Costco stores are estimated to achieve approximately $2 Million per year in sporting goods sales.



- Like sporting goods, the chain toys segment has experienced significant change in recent years, highlighted by the restructuring of Toys 'R Us, the dominant national chain.
- Small, independent retailers classified as primarily toy sellers continue to operate in large numbers, both in San Francisco and elsewhere.
- Average Target stores are estimated to achieve approximately $4.6 Million per year in toy sales: Average Costco stores are estimated to achieve approximately $2 Million per year in toy sales.



- Civic Economics relied extensively on data from QSR Magazine's QSR 50 issue, which estimates sales per store for the top 50 quick service restaurant chains as well as for the fastest growing chains (*www.qsrmagazine.com*).
- Within fast food categories, dominant chains include:
  - Coffee: Starbucks (and Seattle's Best) and Peets – 106 Stores
  - Sandwiches: Subway and Quizno's – 54 Stores
  - Burgers: McDonald's and Burger King – 42 Stores

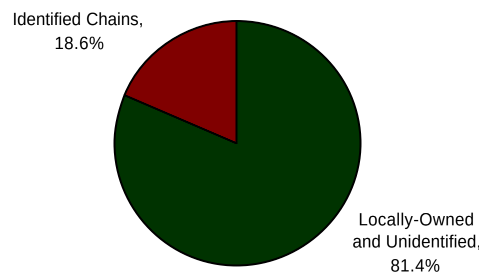
Hardware Market Shares

Locally-owned hardware stores have, in general, fared better in competition with big box chains than other lines of goods facing similarly aggressive competition. Independents, often in affiliation with a cooperative such as Ace or True Value, have found ways to thrive despite ongoing predictions of doom. These retailers have developed a strong niche with convenient locations, personal service, and large selections of small items.

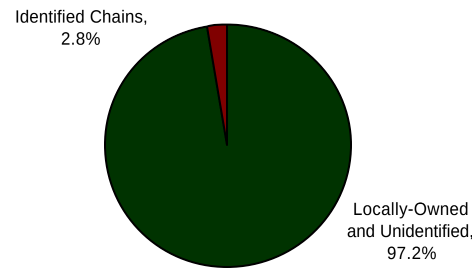
In preparations for this study, both Civic Economics and SFLOMA identified hardware at the outset as an interesting sector for analysis. The ongoing market battles among massive chains, retailer cooperatives, and independents has spawned tremendous changes in the way American consumers shop for hardware, housewares, and related items.

INITIAL HARDWARE FINDINGS

Full Study Area ($981.5 Million)



City of San Francisco ($661.7 Million)



Chain & General Merchant Sales = 125% Corporate Average

During the course of the study, it became obvious that the dataset upon which the market share analysis is built, provided by Claritas, was generating unexpected outcomes. Preliminary analysis indicated relatively tiny market shares for Home Depot and Lowe's in the study area, and extensive efforts to isolate the cause did not measurably reduce that outcome. Further research and discussions with Claritas analysts provided an explanation:

In a typical line of goods, retail activity (sales to end-users) is readily separable from wholesale activity (sales to resellers or large firms). Recent changes in the hardware market, however, have blurred those lines substantially. Big box retail stores seek to attract contractors who traditionally made purchases through wholesalers. Indeed, Home Depot has begun acquiring local wholesalers and bringing them into the company distribution system. Because of this increasing intermixing of retail and wholesale activity, Claritas now aggregates all hardware sales into a single value. In this aggregation, wholesale chains such as Grainger and family-owned lumber yards are swept into the same dataset with the neighborhood hardware store.

The market share methodology was unable to accommodate the inclusion of these wholesalers, as we had no way of estimating the sales per outlet of any number of wholesalers and lumber yards in the study area. However, we may hope to return to the question in the coming years when the industry-wide consolidation and shakeout has run its course.

2 Calculate economic impact of independent businesses

ECONOMIC IMPACT ANALYSIS

This section will show the economic impacts for local merchants relative to national chains and demonstrate the significant positive impacts that additional money retained in the local economy can have in the San Francisco retail market.

Economic Impact Methodology

In developing the methodology utilized in the Austin and Chicago studies discussed above, a new approach was needed in determining the economic impact of locally owned firms compared to national chains. Multipliers reflect practices by industry (i.e. bookstores), and no distinction is made between local versus non-local ownership. That is why Civic Economics undertook the laborious process described in those studies. As we demonstrated, locally-owned firms recirculate substantially more money in the local economy and therefore would have higher multipliers than national chains. So, in order to use nationally recognized multipliers we needed to devise a way to use them to show the differences in impacts between national and independent merchants.

For this study, we have adapted the Local Premium values from the Andersonville study for retailers, restaurants, and service providers on a revenue basis. These values, which quantify money remaining in the local economy after the initial purchase of goods, were applied to total sales for independent and chain merchants in San Francisco. Then, using multipliers specific to the City of San Francisco we were able to calculate the economic impacts of that money. The impacts were measured for both locals and chains based upon how much revenue was spent on labor, contracting services, and profit kept locally. Economic impacts were drawn in three categories - books, retail, and food services. The retail segment was used to calculate economic impacts for both the toy and sporting goods line of goods, while we were able to apply more specific data for the book category based on our previous work. Internet (and book club) sales were assumed to generate no local recirculation of dollars, though in unusual situations some nominal value may be identified.

For each of the lines of goods we calculated economic impacts in four categories:

Economic Output is the total production or sales.

Employment is the total number full-time-equivalents (FTEs) in a given industry.

Labor Income is the amount of salaries and benefits paid to employees.

Retail Sales is a subset of output and measures only the increases in retail activity.

Economic Impact Findings

When looking at the economic impacts that follow it is imperative to remember that these impacts measure only the money left in the local economy *after the initial purchase is made*. The charts on the preceding pages show the dramatic effect that extra money kept in the community by independent retailers can have.

Looking at the book sector, for example, it is easy to see how dramatic an effect Internet sales have on a local economy. Buying a book from an online merchant such as Amazon there is basically no economic impact at all for San Francisco. There are no local employees to pay a salary to, no local services are contracted for, and the profit is divided up in shareholders across the country. Additionally, no sales taxes are collected and the loss of revenue for the city actually results in a loss of sales tax revenue.

The economic impacts for books brings approximately one-third of the revenue back through the economy when purchased from a local merchant as compared to less than twenty percent for national chains. Online merchants themselves bring only nominal value back to the local economy and, when aggregated with national brick and mortar merchants, they recirculate only about eight percent of their revenue.

The same theme plays out for toys and sporting goods as well. However, since these markets have a smaller total sales value in e-commerce, the results are less pronounced.

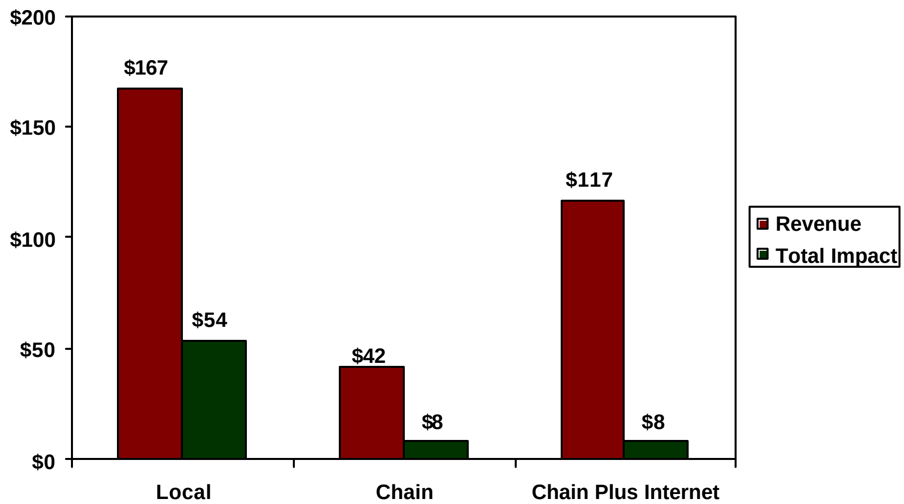
The findings are broken down to show the economic impacts per million dollars of sales. Once again the local merchants generate substantially greater local impact than their national chain competitors. The charts for each product type show the economic advantages locals bring over brick and mortar chains and Internet competitors. The money they keep in the local economy through extra employment, contracted services, and local profit leads to more total output, income, and employment within the City of San Francisco. This, in turn, leads to a further increase in retail sales, which are then taxed to generate additional income for public services.

The final category shown is limited-service restaurants. Dining establishments tend to bring the most economic impact back to the community due to high labor costs. They function almost like a small manufacturing operation, receiving meal ingredients with varying degrees of advance processing, then adding value to them by making complete meals. As a result, the economic impacts as a percent of revenue are much higher than for dining than for the straight retail sectors. These increased economic impacts carry over into the employment, income, and retail sales categories as well.

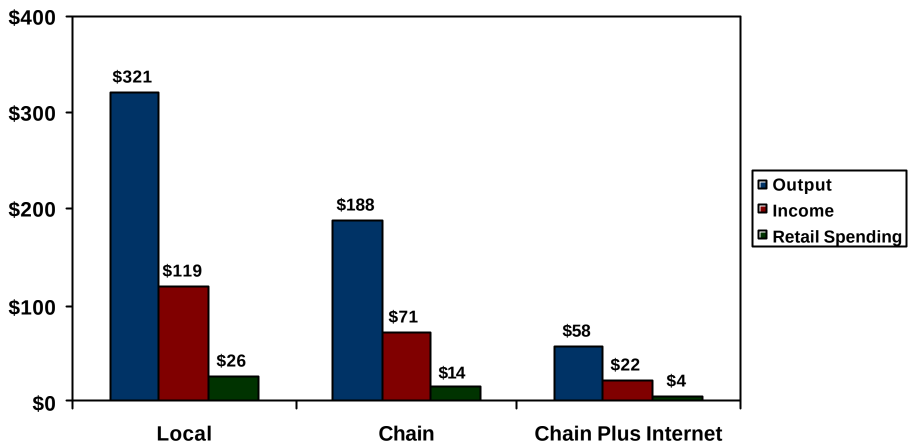
The sector-specific charts that follow highlight the economic impact advantages local merchants bring to the community.

BOOKS

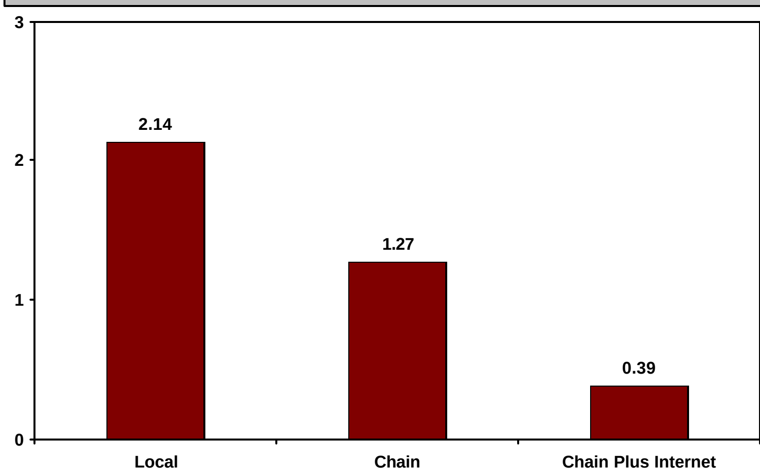
TOTAL REVENUE AND IMPACT (In $ Millions)



ECONOMIC IMPACTS PER $1M REVENUE (in $ Thousands)

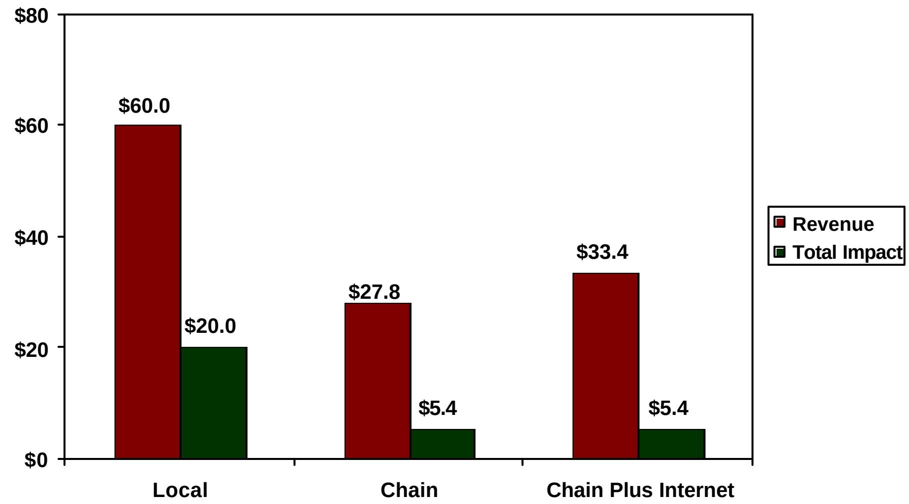


JOBS CREATED PER $1M REVENUE

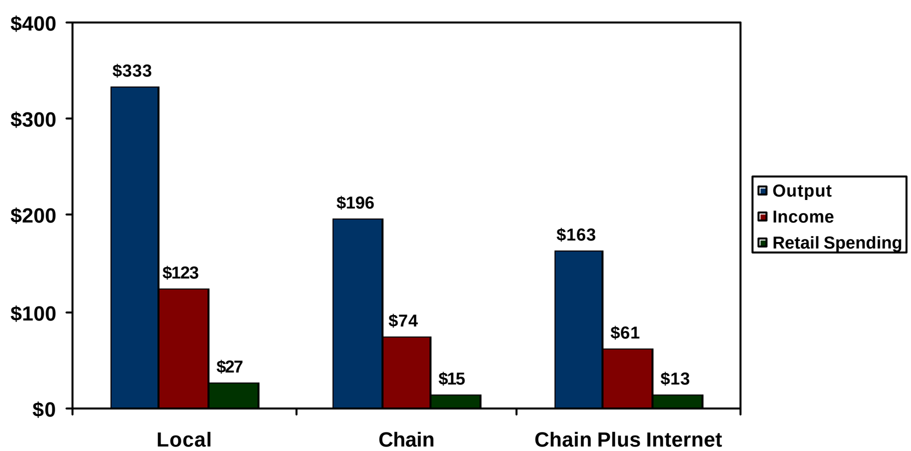


TOYS

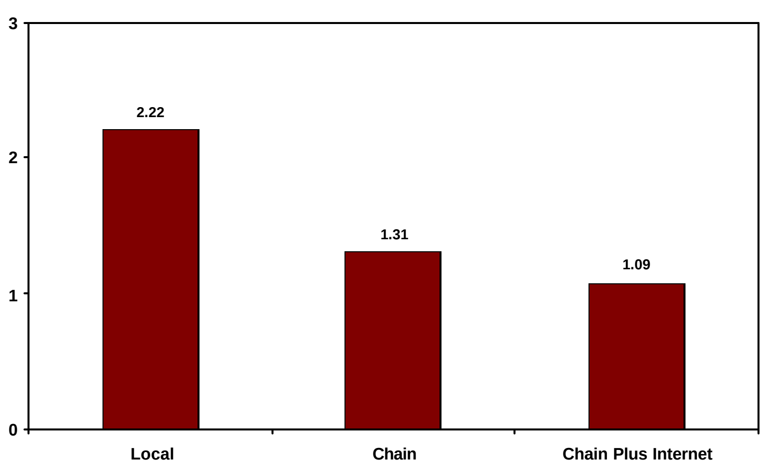
TOTAL REVENUE AND IMPACT (In $ Millions)



ECONOMIC IMPACTS PER $1M REVENUE (in $ Thousands)

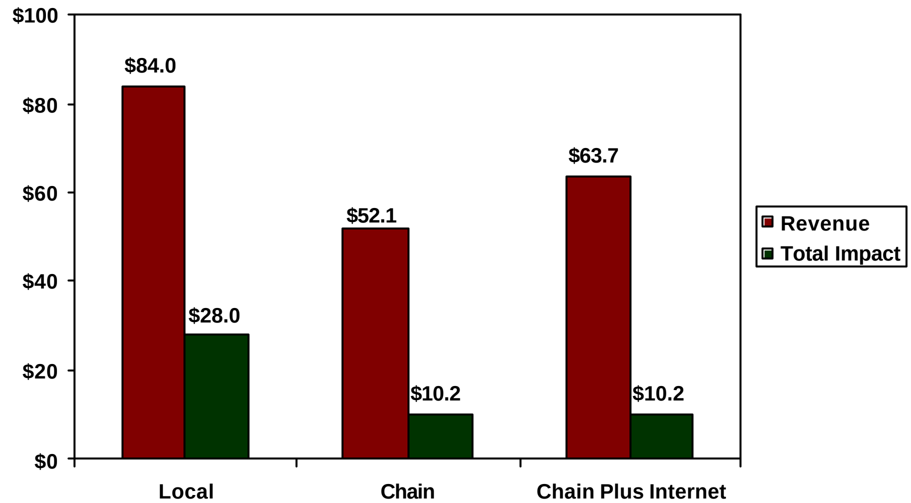


JOBS CREATED PER $1M REVENUE

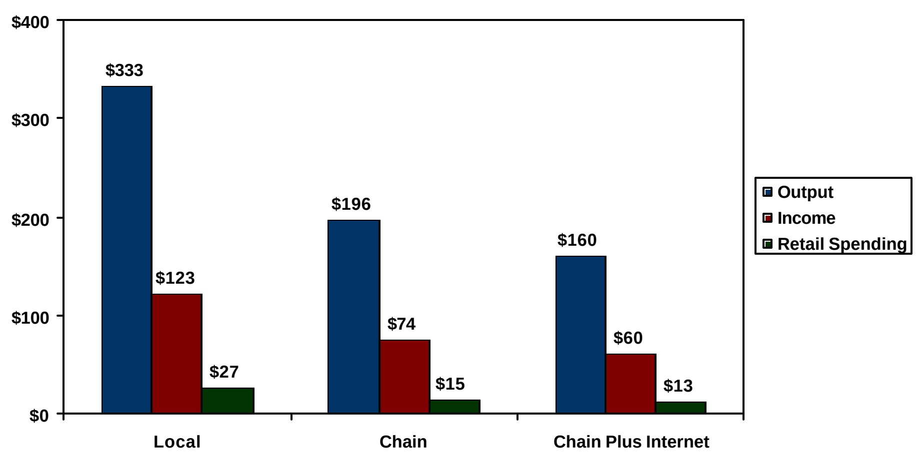


SPORTING GOODS

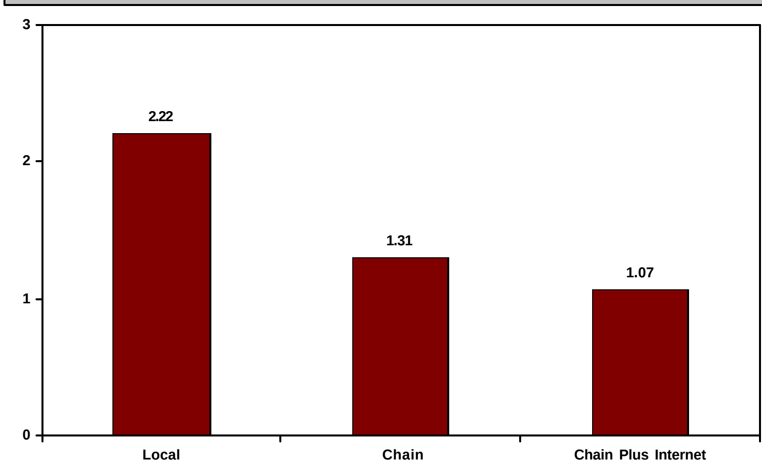
TOTAL REVENUE AND IMPACT (In $ Millions)



ECONOMIC IMPACTS PER $1M REVENUE (in $ Thousands)

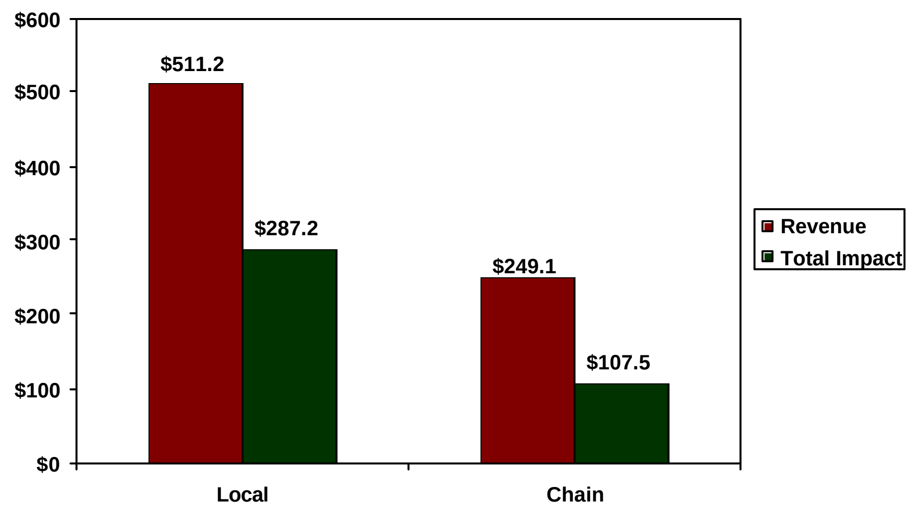


JOBS CREATED PER $1M REVENUE

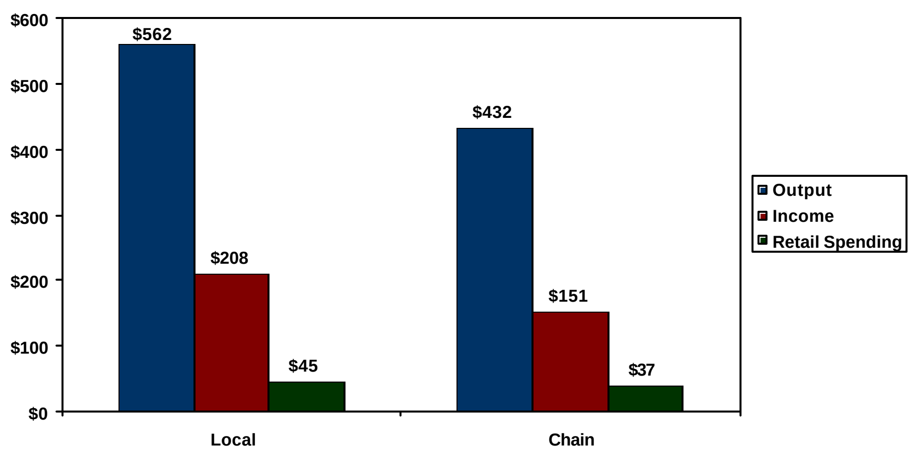


LIMITED SERVICE DINING

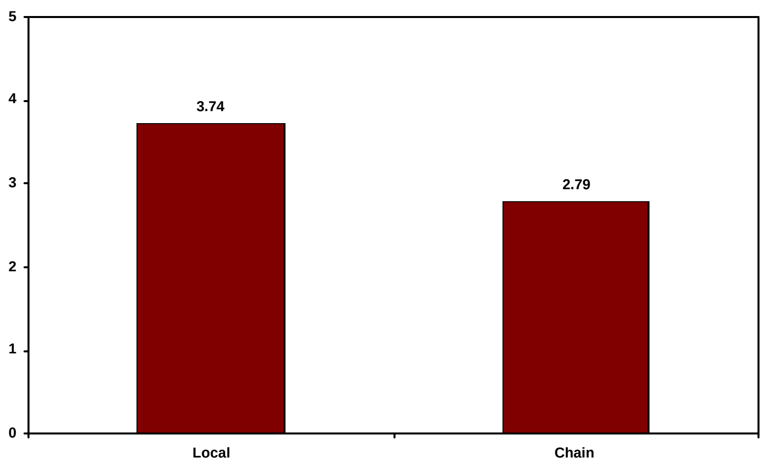
TOTAL REVENUE AND IMPACT (In $ Millions)



ECONOMIC IMPACTS PER $1M REVENUE (in $ Thousands)



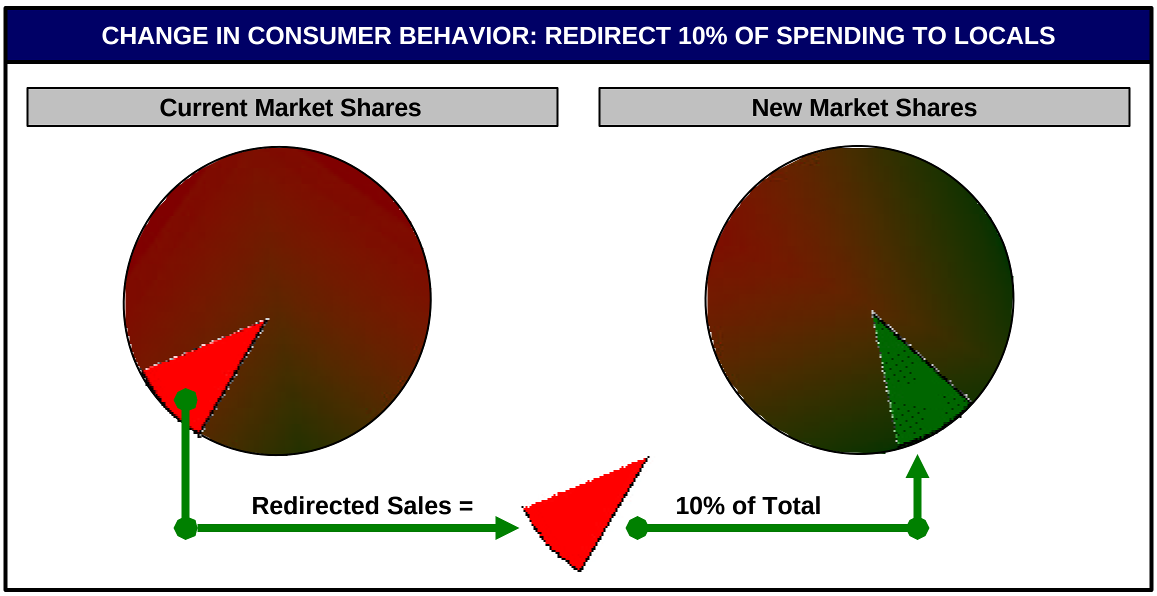
JOBS CREATED PER $1M REVENUE



3 Forecast enhanced impacts associated with redirected consumer spending

CONSUMER GUIDANCE

Having reviewed the existing market shares and enhanced economic impacts associated with locally-owned firms and their chain competitors in four specific sectors, Civic Economics was asked to take the analysis a step further and assess the degree to which modest changes in consumer behavior may bring substantial economic advantages to the community.



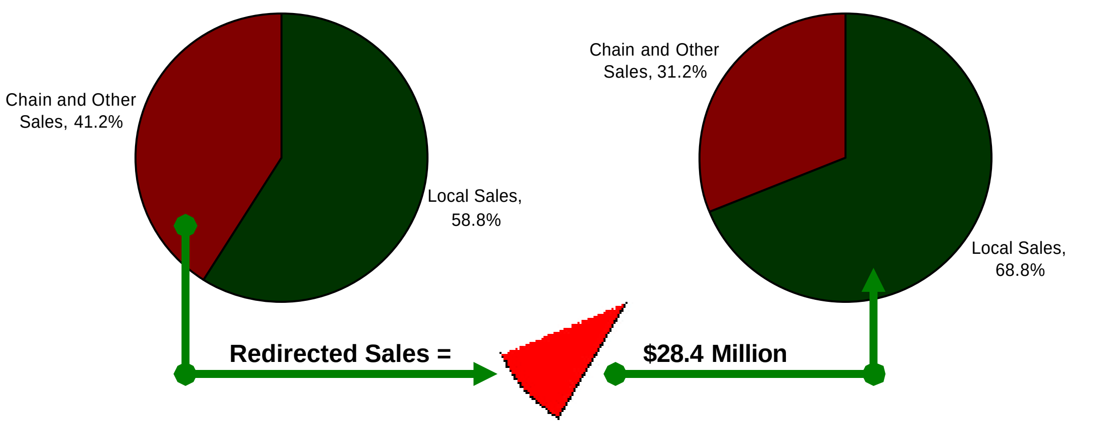
For each line of goods, we have provided an analysis of the economic impact in the City of San Francisco that would be generated from a 10% increase in the market share of locally-owned businesses. Of course, these categories represent a small portion of the total retail and restaurant spending that takes place annually in San Francisco.

Therefore, extending the impact methodology, this section concludes with a chart representing the increased economic impacts in the city if 10% of all retail and restaurant sales were redirected to locally-owned establishments. For individual consumers, that represents just one additional trip to a local merchant for every ten shopping trips. If a household currently buys just two out of ten books or three out of ten sandwiches from local businesses, a conscious effort to nudge those shares slightly will yield increased economic activity and employment and public revenue throughout San Francisco.

BOOKS

REDIRECTING 10% OF SF BOOK SALES TO LOCAL MERCHANTS

Current Market Shares | **New Market Shares**



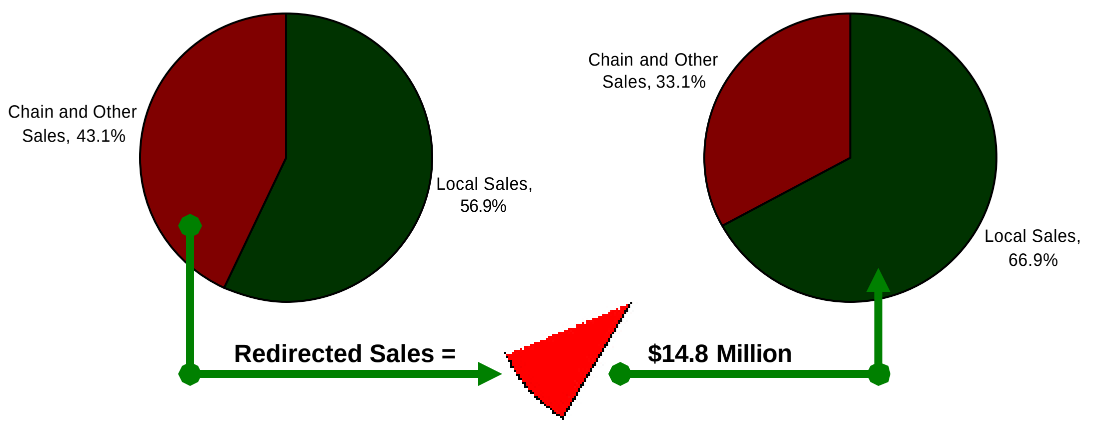
Economic Impacts of Redirected Book Sales

Increased Economic Output	Additional Jobs Created	New Income for Workers	Additional Retail Activity
$ 3,783,984	25	$ 1,341,343	$ 324,861

SPORTING GOODS

REDIRECTING 10% OF SF SPORTING GOODS SALES TO LOCAL MERCHANTS

Current Market Shares | **New Market Shares**



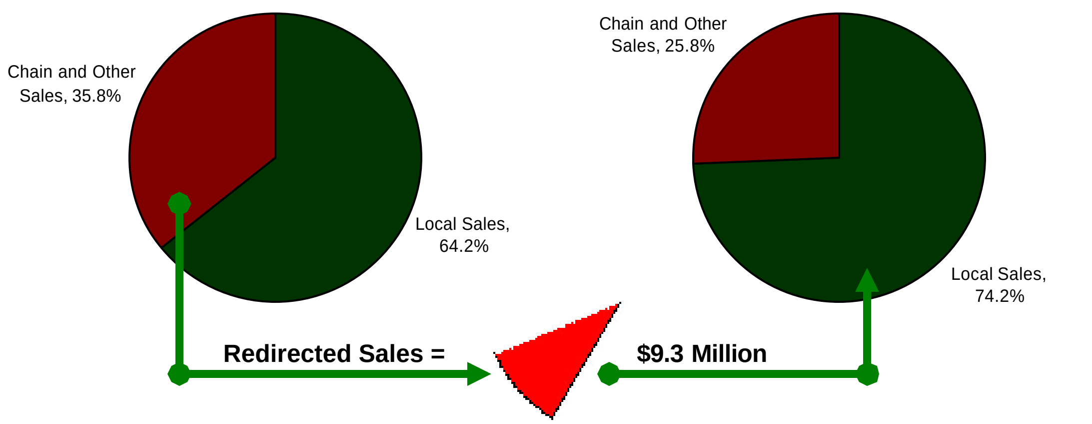
Economic Impacts of Redirected Sporting Goods Sales

Increased Economic Output	Additional Jobs Created	New Income for Workers	Additional Retail Activity
$ 2,026,383	13	$ 728,111	$ 171,084

TOYS

REDIRECTING 10% OF SF TOY SALES TO LOCAL MERCHANTS

Current Market Shares | **New Market Shares**



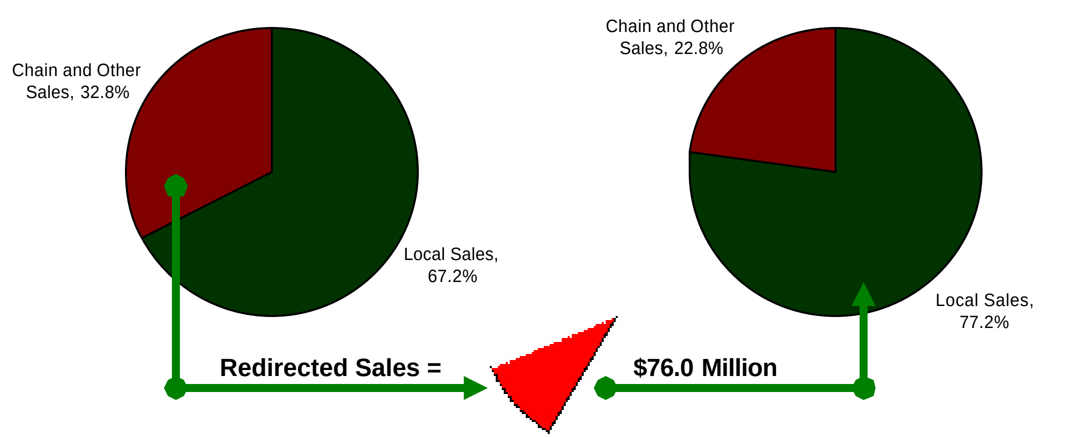
Economic Impacts of Redirected Toy Sales

Increased Economic Output	Additional Jobs Created	New Income for Workers	Additional Retail Activity
$ 1,297,077	8	$ 459,592	$ 107,990

LIMITED SERVICE DINING

REDIRECTING 10% OF SF LIMITED SERVICE DINING SALES TO LOCAL MERCHANTS

Current Market Shares	New Market Shares



Economic Impacts of Redirected Limited Service Dining Sales

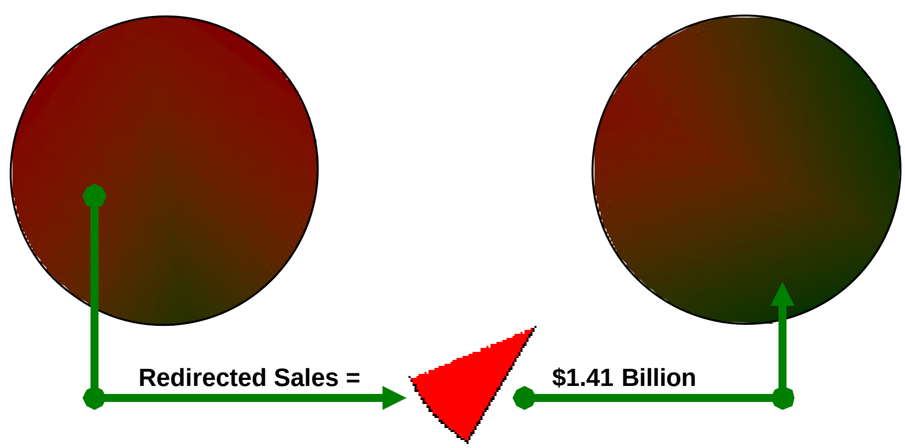
Increased Economic Output	Additional Jobs Created	New Income for Workers	Additional Retail Activity
$ 9,885,260	73	$ 4,304,621	$ 591,573

ALL SAN FRANCISCO RETAIL

REDIRECTING 10% OF ALL SAN FRANCISCO RETAIL SALES TO LOCAL MERCHANTS

Current Market Shares Unknown

New Market Shares Unknown



Economic Impacts of Redirected Retail Sales

Increased Economic Output	Additional Jobs Created	New Income for Workers	Additional Retail Activity
$ 191,984,904	1,295	$ 71,864,175	$ 15,278,772

CONCLUSION

The San Francisco Retail Diversity Study is the first of its kind in the nation.

San Francisco is blessed with a healthy, diverse crop of independent retailers in the lines of goods studied. The same is quite likely true in a variety of other lines of goods and services. Though such a study has not been conducted in any other American market area, we believe that few communities would even approach the market shares found here; in many cities we would struggle to identify any meaningful independent offerings in several lines.

The independent merchants of San Francisco provide the community with a tremendous injection of economic activity. In this analysis, we focused on the positive: increasing independent market share by 10% would yield nearly $200 Million in economic activity and nearly 1,300 new jobs. However, it must be remembered that the reverse is also true: shifting a further 10% of sales to chain merchants would deprive the community of that same $200 Million and put those 1,300 employees out of work.

Though time and funding did not permit a study of market shares over time, there can be little doubt that chain merchants have been garnering increasing market share over the last two decades, in San Francisco as in the rest of the country. No complex analysis is required to recognize that a continuation of this trend would, over some period of time, cost the city millions in economic activity and hundreds of jobs.

To capture the benefits outlined above requires very little of consumers and policy makers. Simply redirecting an occasional shopping trip to a locally owned merchant is all that is asked of consumers. For those purchases where quality goods or knowledgeable service are of particular importance, this small effort may reward the shopper with a more satisfying experience and enhanced value received. Moreover, in price comparisons undertaken by Civic Economics in the past, local merchants have been found to commonly offer equal or better value across a wide range of merchandise provided that she shopper undertakes a bit of comparison shopping.

Similarly little is asked of policy makers. In city after city across the nation, thoughtlessly drafted and applied zoning and permitting processes tend to favor large chains and the developers who build for them. Worse, urban governments all too frequently subsidize developments designed to house a number of chain businesses, further advantaging them relative to existing, locally-based competitors. Local merchants rarely ask for a handout or for special regulatory treatment; they ask only that their competitors be treated the same.

An immediate and easily attainable policy change would target a 10% increase in the local, independent share of public sector purchasing of goods and services. As volume purchasers, the City of San Francisco and the various public institutions in the city can lead the way. Public officials should, of course, actively seek local bidders and provide assistance with the procurement process. But a substantial impact may also be achieved by conscientiously seeking local providers for more routine, no-bid purchases.

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